(32,228)

# SUPREME COURT OF THE UNITED STATES

## OCTOBER TERM, 1926

## No. 661

THE EQUITABLE TRUST COMPANY OF NEW YORK, AS TRUSTEE IN BANKRUPTCY OF KNAUTH, NACHOD & KUHNE, PETITIONER,

*vs.*

THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

INDEX


| | Page |
|---|---|
| Record from the district court of the United States, southern district of New York | 1 |
| Amended petition | 1 |
| Stipulations annexed to petition | 6 |
| Answer to amended petition | 14 |
| Notice of hearing on motion to dismiss | 16 |
| Statement of evidence | 18 |
| Appearances of counsel | 18 |
| Offers in evidence | 19 |
| Testimony of Otto H. Schulz | 40 |
| Colloquy between master and counsel | 109 |
| Testimony of Ralph Dawson | 113 |
| Colloquy between master and counsel | 126 |
| Testimony of Otto H. Schulz (recalled) | 129 |


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Page

Claimant's Exhibit 1—Extract from "List of Foreign Correspondents" ..... 140
Claimant's Exhibit 2—Forms of drafts and advices ..... 158
Claimant's Exhibits 3, 4, 5, 6, 6A, B, C, D, E—Checks, advices, and drafts ..... 161
Claimant's Exhibits 7, 8, and 9—Statements ..... 169
Claimant's Exhibits 10-19—Correspondence between M. S. Borland and Banca Commerciale Italiana ..... 174
Trustee's Exhibits 1 and 2—Statements ..... 186
Trustee's Exhibits 3 and 4—Forms ..... 192
Trustee's Exhibit 5—Statement ..... 193
Trustee's Exhibits 6 and 7—Correspondence between M. S. Borland and Banca Commerciale Italiana ..... 195
Report and opinion of special master ..... 198
Exceptions to report of special master ..... 218
Notice of motion for order confirming report of special master ..... 222
Opinion, Knox, J. ..... 223
Order confirming report of special master ..... 225
Petition for appeal and order allowing same ..... 227
Notice of appeal ..... 230
Citation ..... 231
Assignments of error ..... 232
Notice of filing petition to revise ..... 235
Petition to revise ..... 237
Exhibit A—Order confirming report of special master ..... 242
Stipulations re transcript of record ..... 244
Clerk's certificate ..... 246
Proceedings in United States circuit court of appeals, second circuit ..... 247
Opinion, Hand, J. ..... 247
Judgment ..... 258
Clerk's certificate ..... 259
Order allowing certiorari ..... 260

**Amended Petition.**

# United States District Court,

SOUTHERN DISTRICT OF NEW YORK.

| | |
|---|---|
| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, JAMES F. SHAW, ROLLIN C. NEWTON, HERBERT B. SMITHERS, JOHN R. HALL, MARY W. KNAUTH, and THEODORE W. KNAUTH, trading as partners under the firm name and style of KNAUTH, NACHOD & KUHNE, and OSCAR L. GUBELMAN, JAMES F. SHAW, ROLLIN C. NEWTON and JOHN R. HALL, individually,<br>Bankrupts,<br>and<br>HERBERT B. SMITHERS, MARY W. KNAUTH and THEODORE W. KNAUTH,<br>Alleged Bankrupts. | In Bankruptcy.<br>No. 34,996. |





TO THE HONORABLE JUDGES OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK:

The amended petition of First National Bank of Trinidad, Colorado, by its attorneys, O'Brien, Boardman, Parker & Fox, respectfully shows:

1. Upon information and belief, that on or

about June 15, 1923, an involuntary petition in bankruptcy was filed in this Court against the above-named firm and the members thereof individually, and said firm and the members thereof were thereafter, by orders of this Court, duly adjudicated bankrupts.

2. Upon information and belief, Middleton S. Borland, Esq., was, by order of this Court, duly appointed Receiver in Bankruptcy herein and duly qualified as such, and took possession of the assets of the said bankrupts. Thereafter the said Middleton S. Borland was duly elected Trustee of the estate of the said bankrupts, duly qualified as such, and as such Trustee took possession of all the assets of said bankrupts.

3. Petitioner is a corporation duly organized under and by virtue of the National Banking Laws.

4. Prior to May 19, 1923, the bankrupts, in order to induce petitioner to enter into trade relations with them, offered to accept from petitioner from time to time sums of money and to use the same for the payment of drafts to be drawn by petitioner upon certain designated foreign correspondents of bankrupts and advised by petitioner to bankrupts.

5. Heretofore and on or about May 19, 1923, petitioner, in acceptance of said offer, drew its draft No. 61,161 on Banca Commerciale Italiana at Sassari, Italy, wherein and whereby it directed said Banca Commerciale Italiana to pay to Zara Sanna Giovanni, upon presentment of said draft by her, 24,360 lire, and on or about the same day petitioner delivered to the bankrupts the sum of $1,191.20, to be used for the payment of said draft

when presented and not otherwise, and the bankrupts accepted said sum and agreed with petitioner to use the same for the payment of said drafts when presented, and for no other purpose. 7

6. The bankrupts failed to cause said sum of $1,191.20 or any part thereof to be used for the payment of said draft when presented and, by reason thereof, the said draft, although duly presented by said Zara Sanna Giovanni, was not paid when presented but was then dishonored.

7. Upon information and belief, the said sum of $1,191.20, so delivered to the bankrupts, has come into and now is in the possession and control of the said Trustee, who has refused to return the same, although duly demanded. 8

FOR A SEPARATE AND COMPLETE COUNT.

8. Petitioner realleges each and every allegation contained in paragraphs of the amended petition numbered "1," "2," "3," "4" and "5."

9. Upon information and belief, there existed at all the times herein mentioned, to the knowledge of the bankrupts, a custom on the part of Banca Commerciale Italiana to charge the account of the bankrupts with the amount of drafts drawn against it upon receipt of advice thereof from the bankrupts and thereupon to set aside and appropriate said amount to the payment of said drafts when presented. 9

10. Upon information and belief, the bankrupts, on or about May 22, 1923, notified Banca Commerciale Italiana of the drawing of the aforesaid draft upon it and requested Banca Commerciale Italiana to charge the same to their account; upon

information and belief, that the said advice was received by Banca Commerciale Italiana on or about June 4, 1923, and thereupon the said Banca Commerciale Italiana, with the knowledge and acquiescence of the bankrupts, set aside in a separate fund and appropriated to the payment of said draft the sum of 24,360 lira, and charged the same against the account of the bankrupts.

11. Upon information and belief, thereafter, and while said lira remained so set apart and appropriated by said Banca Commerciale Italiana to the payment of the aforesaid draft when presented, but before presentation thereof, the receiver of the estate of the bankrupts, theretofore appointed, instructed and directed Banca Commerciale Italiana not pay the said draft when presented and to return the amount so set apart and appropriated to the receiver.

12. Upon information and belief, the said moneys so set apart and appropriated to the payment of said draft were thereafter, and pursuant to said direction of the receiver, returned as directed by the receiver and came into, and now are, in the trustee's possession and control, and the trustee has refused to return the same, although duly demanded.

13. Upon information and belief, the said draft was duly presented by said Zara Sanna Giovanni, was not paid when presented, and was then dishonored, of which notice was duly given to the trustee herein.

Wherefore, petitioner prays that it be adjudged that petitioner is entitled to, and has a lien upon,

the moneys in the hands of the Trustee for the amount of $1,191.20 with interest thereon from May 19, 1923, superior to any and all rights of the bankrupts, or their Trustee or any other creditor herein, and that the Trustee be decreed to pay said sum with interest to petitioner out of the moneys in his hands.

O'Brien, Boardman, Parker & Fox,
Attorneys for Petitioner,
Office and Post Office Address.
120 Broadway,
New York City. 14

State of New York, }
County of New York, } ss.:

Wm. De Forest Manice, being duly sworn, deposes and says:

That he is a member of the firm of O'Brien, Boardman, Parker & Fox, 120 Broadway, New York City, attorneys for the petitioner herein; that he has read the foregoing amended petition and knows the contents thereof; that the same is true to his knowledge, except as to the matters therein stated to be alleged upon information and belief, and that as to those matters he believes it 15
to be true.

That the sources of deponent's information and the grounds of his belief are communications received by him from petitioner and copies of communications between the bankrupts and petitioner, together with investigations made by deponent and accountants engaged by his firm of the books, records and files of the bankrupts in the possession of the Trustee.

Deponent further says, that the reason why

16 *Stipulation Annexed to Amended Petition.*

this verification is not made by the petitioner and is made by him is that the petitioner is a foreign corporation which does not maintain an office or agent in the State of New York.

WM. DE FOREST MANICE.

Sworn to before me this 20th
day of June, 1924.

WILLIAM H. VOGT,
[SEAL.] Notary Public, Queens County
Queens County No. 1154,
17 Certificate filed in New York Co.
New York Co. Clerk's No. 114,
New York Co. Register's No. 6036,
Commission expires March 30, 1926.

## UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

| | |
|---|---|
| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, *et al.*, trading as KNAUTH, NACHOD & KUHNE,<br>18 Bankrupts,<br>and<br>MARY W. KNAUTH,<br>Alleged Bankrupt. | In Bankruptcy No. 34996. |

WHEREAS, Messrs. O'Brien, Boardman, Parker & Fox, hereinafter called the "Attorneys," are attorneys for, and represent, and may hereafter represent a large number of banks and other

claimants against the above named bankrupts, all of which claimants desire to assert reclamation claims against the estate of said bankrupts, and

WHEREAS, an order has been entered herein providing that all reclamation claims against said bankrupts must be filed on or before June 19, 1924, or be forever barred, and

WHEREAS, the inconvenience of filing a large number of reclamation petitions setting forth individual claims, is recognized by the parties hereto and it is also recognized that a great number of 20
reclamation claims represented by the Attorneys will naturally fall into certain classes capable of being represented by typical reclamation petitions,

NOW, THEREFORE, it is agreed by and between the Attorneys and Middleton S. Borland, Esq., trustee of the bankrupts, hereinafter referred to as the "Trustee," as follows:

1. The attorneys may file with the Special Master and with the trustee herein, prior to June 19, 1924, a reclamation petition or reclamation petitions based upon such claims and pursuant to such legal theories as the attorneys may deem 21
proper or advisable. Such petition or petitions are hereinafter referred to as "typical petitions."

2. With such typical petitions the attorneys may also serve upon the Special Master and the trustee herein, a list of the names of claimants represented by said attorneys with a proper designation after each name appearing on such list stating what part of each claimant's claim falls under each of the typical petitions and there-

22 *Stipulation Annexed to Amended Petition.*

upon the typical petition so designated shall be deemed a petition upon so much of each said claim in favor of such claimant.

3. It is understood that any statements of names, addresses, dates, amounts or other formal information of a similar character contained in the typical petitions, identifying the particular transaction or transactions set forth in the typical petitions, shall not be deemed applicable to the items constituting the claims mentioned on said list, but that in each case the attorneys will supply
23 the receiver on demand with such identifying information applicable to each of the claims mentioned on said list.

4. It is understood, however, that the typical petitions and the designation with respect to each claim heretofore referred to, shall be filed with the trustee and with the Special Master on or before the 19th day of June, 1924, in accordance with the order of the United States District Court duly entered and nothing herein shall be deemed to be a waiver of that requirement.

Dated, New York, June 3, 1924.

24 O'Brien, Boardman, Parker & Fox,
Attorneys.
Middleton S. Borland, Trustee.
By Rosenberg & Ball,
Attorneys.

*Stipulation Annexed to Amended Petition.* 25

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

| | |
|---|---|
| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, JAMES F. SHAW, ROLLIN C. NEWTON, HERBERT B. SMITHERS, JOHN R. HALL, MARY W. KNAUTH, and THEODORE W. KNAUTH, trading as partners under the firm name and style of KNAUTH, NACHOD & KUHNE, and OSCAR L. GUBELMAN, JAMES F. SHAW, ROLLIN C. NEWTON and JOHN R. HALL, individually,<br>Bankrupts,<br>*and*<br>HERBERT B. SMITHERS, MARY W. KNAUTH and THEODORE W. KNAUTH,<br>Alleged Bankrupts. | In Bankruptcy No. 34,996. |

26

27

List of claimants represented by Messrs. O'Brien, Boardman, Parker & Fox, attorneys, attached to the foregoing typical petition of the First National Bank of Trinidad, Colorado, pursuant to the stipulation between said Messrs. O'Brien, Boardman, Parker & Fox, attorneys for claimants, and Middleton S. Borland, Trustee in Bankruptcy, herein, dated June 3, 1924, a copy of which stipulation is hereto attached. All of

28 *Stipulation Annexed to Amended Petition.*

each claimants claim falls under the said foregoing typical petition.

| | Drafts |
|---|---|
| Aberdeen National Bank, The, Aberdeen, Wash. | $ 1,141.22 |
| Alexander & Company, Monongahela, Pa. | 4,364.50 |
| Alliance First National Bank, Alliance, Ohio | 1,061.34 |
| Ambridge Savings & Trust Company, Ambridge, Pa. | 1,205.70 |
| American National Bank, Newark, N. J. | 971.60 |
| American State Bank of Highland Park, Highland Park, Mich. | 4,202.68 |
| Arkansas National Bank, Hot Springs, Ark. | 1,940.38 |
| Atlantic National Bank, Atlantic, Iowa | 580.32 |
| Atlas Exchange National Bank, Chicago, Ill. | 18,777.60 |
| Banca Joseph M. Vigliotti, Detroit, Mich. | 2,020.06 |
| 29 Bank of Bay Biscayne, Miami, Fla. | 694.78 |
| Bank of Detroit, Detroit, Mich. | 14,935.39 |
| Bank of Eureka, Eureka, Cal. | 6,087.17 |
| Bank of Hamilton, Hamilton, Ontario | 4,511.13 |
| Bank of Mill Creek, Mill Creek, W. Va. | 849.80 |
| Bank of North America & Trust Company, Philadelphia, Pa. | 4,452.13 |
| Bank of Palo Alto, Palo Alto, Cal. | 2,295.67 |
| Bank of Watertown, Watertown, Wisc. | 119.22 |
| Bank of Wisconsin, Madison, Wisc. | 3,372.38 |
| Bernheim, Alfred & Sons, Brooklyn, N. Y. (Oscar Bernheim) | 1,608.20 |
| Brattstrom & Company, Seattle, Wash. | 309.28 |
| Bridgeport Trust Company, The, Bridgeport, Conn. | 1,780.78 |
| Brighton Bank & Trust Company, The, Cincinnati, Ohio | 554.51 |
| Citizens & Manufacturers National Bank, Waterbury, Conn. | 2,519.55 |
| 30 Citizens National Bank, The, Monessen, Pa. | 1,919.00 |
| Citizens State Bank, Sheridan, Wyo. | 185.90 |
| Citizens Title & Trust Company, Uniontown, Pa. | 382.50 |
| Citizens Trust & Savings Bank, Indiana Harbor, Ind. | 1,989.77 |
| City Bank, The, Milwaukee, Wisc. | 4,449.13 |
| City National Bank, The, Bridgeport, Conn. | 5,187.38 |
| City Trust & Savings Bank, Dayton, Ohio | 822.50 |
| City Trust & Savings Bank, E. Youngstown, Ohio | 6,246.11 |
| Coffman-Dobson Bank & Trust Company, Chehalis, Wash. | 530.13 |
| Colonial Trust Company, The, Farrell, Pa. | 415.45 |
| Commerce Guardian Trust & Savings Bank, Toledo, Ohio | 15,341.52 |
| Commercial National Bank, Los Angeles, Cal. | 2,529.51 |

| | Drafts |
|---|---|
| Commercial National Bank, Youngstown, Ohio | 21,898.45 |
| Cuipo, Louis, Perth Amboy, N. J. | 1,635.47 |
| Dayton National Bank, Dayton, Ohio | 1,799.82 |
| Denver National Bank, The, Denver, Colo. | 869.56 |
| Depositors Savings & Trust Co., The, Akron, Ohio | 1,593.68 |
| De Santis, Louis—Bank of Canton, Canton, Ohio | 13,425.96 |
| Di Claudio, Frank, Jeanette, Pa. | 911.00 |
| Dixon Savings Bank, The, Dixon, Iowa | 241.41 |
| Drovers Trust & Savings Bank, Chicago, Ill. | 1,541.33 |
| Elizabeth Trust Company, Elizabeth, N. J. | 913.12 |
| Elyria Savings & Trust Company, The, Elyria, Ohio | 6,547.10 |
| Exchange National Bank, The, Spokane, Wash. | 584.04 |
| Farmers & Merchants National Bank, Los Angeles, Cal. | 7,036.06 |
| Farmers & Merchants National Bank, The, Oakland, Neb. | 462.31 32 |
| Farmers National Bank, Beaver Falls, Pa. | 1,684.75 |
| Farmers State Bank, Clarkson, Neb. | 25.00 |
| Fayette Title & Trust Company, Uniontown, Pa. | 6,679.86 |
| Fifth Third National Bank, Cincinnati, Ohio | 4,789.25 |
| First National Bank of Brooklyn, Brooklyn, N. Y. | 4,983.01 |
| First National Bank, Canton, S. D. | 25.20 |
| First National Bank, Chisholm, Minn. | 144.45 |
| First National Bank, Christopher, Ill. | 2,272.28 |
| First National Bank, Clifton, Kans. | 36.26 |
| First National Bank, Denver, Colo. | 3,328.40 |
| First National Bank, Ely, Minn. | 341.49 |
| First National Bank, Erie, Pa. | 6,261.83 |
| First National Bank, Farrell, Pa. | 837.08 |
| First National Bank, Gary, Ind. | 2,450.86 |
| First National Bank, Hazleton, Pa. | 2,240.92 |
| First National Bank, Herrin, Ill. | 675.87 |
| First National Bank, Highland Falls, N. Y. | 8,063.18 33 |
| First National Bank, Jewell, Iowa | 2,023.98 |
| First National Bank of Lansford, Lansford, Pa. | 120.84 |
| First National Bank of Logan, Logan, W. Va. | 3,196.33 |
| First National Bank of Los Angeles, Los Angeles, Cal. | 2,367.03 |
| First National Bank, Missoula, Mont. | 5,727.56 |
| First National Bank, Newport News, Va. | 521.07 |
| First National Bank, New Salem, Pa. | 1,953.00 |
| First National Bank, Philadelphia, Pa. | 3,575.91 |
| First National Bank, Roanoke, Va. | 1,024.65 |
| First National Bank, Sharon, Pa. | 3,002.69 |
| First National Bank, Springfield, Ill. | 960.41 |
| First National Bank, Trinidad, Colo. | 3,765.09 |
| First National Bank, Two Harbors, Minn. | 504.02 |

34 *Stipulation Annexed to Amended Petition.*

| | Drafts |
|---|---|
| First National Bank, Welch, W. Va. | 9,924.37 |
| First National Bank, El Paso, Texas | 8,882.17 |
| First National Bank, Gothenburg, Neb. | 1,520.46 |
| Fletcher American National Bank, The, Indianapolis, Ind. | 726.35 |
| Fourth National Bank, Grand Rapids, Mich | 2,808.37 |
| First National Bank, Newman Grove, Neb. | 18.18 |
| Gretna Exchange & Savings Bank, Gretna, La. | 362.83 |
| Haberfeld, Bernard—All Nations Bank, Rochester, Pa. | 1,458.00 |
| Highland Park State Bank, Highland Park, Mich. | 23,365.99 |
| Hoboken Trust Company, Hoboken, N. J. | 3,014.29 |
| Humboldt Bank, San Francisco, Cal. | 5,619.26 |
| Ilasco Supply Company, Ilasco, Mo. | 1,948.82 |
| Indiana Harbor National Bank, Indiana Harbor, Ind. | 423.83 |
| 35 International State Bank, Raton, New Mexico | 667.15 |
| Iowa National Bank, Davenport, Iowa | 190.40 |
| Ironbound Trust Company, Newark, N. J. | 538.25 |
| Jackson State National Bank & State Savings Bank & Trust Company, Jackson, Miss. | 3,316.51 |
| Jacobs, Ward W., & Company, Hartford, Conn. | 2,326.61 |
| Jefferson Gravois Bank, St. Louis, Mo. | 748.45 |
| Johnsonburg National Bank, Johnsonburg, Pa. | 508.75 |
| Jubelirer Brothers, Brownsville, Pa. | 174.65 |
| Katz, Arnold Company, Philadelphia, Pa. | 8,811.92 |
| Klein, H., Bayonne, N. J. | 1,574.25 |
| La Grande National Bank, La Grande, Ore. | 4,979.94 |
| Liberty Insurance Bank, Louisville, Ky. | 4,222.93 |
| Linares & Remigno, Bankers, Paterson, N. J. | 3,385.46 |
| Lincoln Alliance Bank, Rochester, N. Y. | 804.01 |
| Liberty Savings Bank & Trust Company, Memphis, Tenn. | 8,063.53 |
| 36 Marine National Bank, Seattle, Wash. | 3,174.12 |
| Masontown National Bank, The, Masontown, Pa. | 4,511.46 |
| Merchants & Manufacturers Bank, Milwaukee, Wisc. | 1,202.34 |
| Merchants & Miners State Bank, Hibbing, Minn. | 2,198.26 |
| Merchants & Miners National Bank, Ironwood, Mich. | 7,166.07 |
| Merchants National Bank of St. Paul, St. Paul, Minn. | 1,089.30 |
| Mid-City Trust & Savings Bank, Chicago, Ill. | 11,026.13 |
| Mosser Company, The Louis, Pittsburgh, Pa. | 2,203.11 |
| Morelli State Bank, The, Steubenville, Ohio | 3,304.37 |
| Mountain Trust Bank, Roanoke, Va. | 687.64 |
| National Bank of Commerce, The, Seattle, Wash. | 1,291.93 |
| New Britain Trust Company, The, New Britain, Conn. | 2,445.42 |
| Norwegian American Line, John T. Moe, Agent, Duluth, Minn. | 900.10 |
| Ohio Savings Bank & Trust Co., The, Toledo, Ohio | 1,585.37 |

| | Drafts | |
|---|---|---|
| Padula, James V., Newark, N. J. | 5,850.00 | |
| Passaic National Bank & Trust Co., Passaic, N. J. | 1,803.39 | |
| Pecoraro, Gennaro, Italian Banker, Springfield, Mass. | 107.60 | |
| Peoples Bank Company, The, Alliance, Ohio | 593.49 | |
| Peoples Bank & Savings Co., The, Cincinnati, Ohio | 2,036.99 | |
| Peoples National Bank, Ellwood City, Pa. | 1,715.74 | |
| Peoples National Bank, Steubenville, Ohio | 3,239.20 | |
| Peoples Savings & Trust Company of New Castle, New Castle, Pa. | 24,676.66 | |
| Peoples State Bank, The, Gary, Ind. | 2,728.55 | |
| Pittsburgh State Bank, Pittsburgh, Pa. | 4,694.48 | |
| Putnam Trust Company, Greenwich, Conn. | 1,375.59 | |
| Quarter Savings & Trust Company, Wheeling, W. Va. | 1,837.00 | |
| Reading National Bank, The, Reading, Pa. | 5,549.41 | |
| Red Lodge State Bank, The, Red Lodge, Mont. | 67.95 | 38 |
| Rock Springs National Bank, Rock Springs, Wyo. | 2,942.79 | |
| Roth & Son, Joseph, McKeesport, Pa. | 3,729.31 | |
| Security State Bank, Omaha, Neb. | 2,089.66 | |
| Shigo, John, Freeland, Pa. | 176.00 | |
| Shigo, John, Lansford, Pa. | 2,997.00 | |
| State Bank of Concrete, Concrete, Wash. | 402.00 | |
| State Bank of Grand Island, Grand Island, Neb. | 314.25 | |
| State Bank of Lyons, The, Lyons, Colo. | 179.64 | |
| State Savings & Trust Company, The, Indianapolis, Ind. | 3,514.19 | |
| State Savings Bank & Trust Company, Moline, Ill. | 3,494.90 | |
| Steubenville Bank & Trust Company, The, Steubenville, Ohio | 616.25 | |
| *Strandberg, McGreevy & Company, Kansas City, Mo. | 1,212.76 | |
| Traders Bank, Lexington, Mo. | 440.88 | |
| Union Savings Bank & Trust Company, Cincinnati, Ohio | 5,276.17 | 39 |
| Union Savings Bank, Youngstown, Ohio | 11,853.77 | |
| United Savings Bank & Trust Company, San Francisco, Cal. | 3,848.11 | |
| Vermilion National Bank, Vermilion, S. D. | 59.13 | |
| Wallace Bank & Trust Company, Wallace, Idaho | 423.07 | |
| Washington Bank & Trust Company, Indianapolis, Ind. | 41.05 | |
| Washoe County Bank, Reno, Nev. | 975.07 | |
| Wells Fargo Bank & Union Trust Co., San Francisco, Cal. | 6,813.82 | |
| Western Bank & Trust Company, Cincinnati, Ohio | 1,522.77 | |
| Williamsburg Savings Bank, Brooklyn, N. Y. | 2,779.13 | |
| Youngstown State Bank, Youngstown, Ohio | 107.60 | |
| | $503,851.99 | |

*Later withdrawn.

40

## Answer to Amended Petition.

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

| | |
|---|---|
| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, JAMES F. SHAW, ROLLIN C. NEWTON, HERBERT B. SMITHERS, JOHN R. HALL, MARY W. KNAUTH and THEODORE W. KNAUTH, trading as co-partners under the firm name and style of KNAUTH, NACHOD & KUHNE and OSCAR L. GUBELMAN, JAMES F. SHAW, ROLLIN C. NEWTON, JOHN R. HALL and THEODORE W. KNAUTH, individually,<br>Bankrupts,<br>and<br>MARY W. KNAUTH,<br>Alleged Bankrupt. | In Bankruptcy. No. 34,996. |

41

42

TO THE HONORABLE JUDGES OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK.

MIDDLETON S. BORLAND, as Trustee in Bankruptcy herein, by Rosenberg & Ball, his attorneys, answering the amended petition of the claimant, First National Bank of Trinidad, alleges:

1. That he is without knowledge as to the truth

of any of the allegations contained in paragraphs "4," "5," "6," "7," "8," "9," "10," "11," "12" and "13" of the petition.

WHEREFORE the Trustee prays that an order be entered dismissing the petition with costs.

Dated, New York, October 23, 1924.

ROSENBERG & BALL,
Attorneys for the Trustee,
Office and Post Office Address,
74 Broadway,
Borough of Manhattan, 44
City of New York.

STATE, COUNTY AND CITY OF NEW YORK, } ss.:
Southern District of New York.

MIDDLETON S. BORLAND, being duly sworn, deposes and says that he has read the foregoing answer and knows the contents thereof and that the same is true to the best of his knowledge, information and belief.

MIDDLETON S. BORLAND.

Sworn to before me this
24th day of October, 1924. 45

ANNA M. MALLOY,
Notary Public 44, New York County
N. Y. Register's No. 6022, Term expires March 30, 1926.

46 **Notice of Hearing to Dismiss Claim.**

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

| | |
|---|---|
| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL, MARY W. KNAUTH, and<br>47 THEODORE W. KNAUTH, doing business as co-partners under the firm name and style of KNAUTH, NACHOD & KUHNE, and OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL and THEODORE W. KNAUTH, individually,<br>Bankrupts,<br>and<br>MARY W. KNAUTH,<br>Alleged Bankrupt. | In Bankruptcy. No. 34,996. |

48

SIRS:

Please take notice that a hearing will be had on the claim filed by you herein before Robert P. Stephenson, Esq., as Special Master, at his office No. 32 Broadway, Borough of Manhattan, City of New York, on the 17th day of September, 1924, at 10:30 o'clock in the forenoon, and a motion will then and there be made to dismiss said claim,

 49

and for such other and further relief as to the Court may seem just and proper.

New York, August 29, 1924.

Yours, etc.,

ROSENBERG & BALL,
Attorneys for Middleton S. Borland, as Trustee,
Office and P. O. Address,
No. 74 Broadway,
Borough of Manhattan, 50
City of New York.

To MESSRS. O'BRIEN, BOARDMAN, PARKER & FOX,
Attorneys for First National Bank of Trinidad, Col.
120 Broadway,
New York City.

51

52

## Minutes of Hearing.

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK,

In Bankruptcy.

Before ROBERT P. STEPHENSON, Esq., Special Master.

53 In the Matter

*of*

KNAUTH, NACHOD & KUHNE,
Bankrupts.

32 BROADWAY, NEW YORK CITY,

October 24th, 1924; 10.30 A. M.

HEARING ON RECLAMATION OF FIRST NATIONAL BANK OF TRINIDAD, COLORADO,

Proceeded pursuant to adjournment.

54 MESSRS. ROSENBERG & BALL, Attorneys for Trustee;

BY GODFREY GOLDMARK, Esq., GEORGE G. ERNST, Esq., and RALPH F. COLIN, Esq., Of Counsel.

MESSRS. O'BRIEN, BOARDMAN, PARKER & FOX, Attorneys for Claimant.

BY WILLIAM DE FOREST MANICE, Esq., and GEORGE TROSK, Of Counsel.

ALLEN R. MEMHARD, Esq., Of Counsel for Claimant.

Mr. Memhard.—I would like to call your 55
Honor's attention to the fact that Paragraphs 1, 2 and 3 of the Petition are admitted.

The Master.—But the answer denies Paragraph 8, which realleges Paragraphs 1, 2 and 3 so, as the pleadings stand, the answer denies Paragraphs 1, 2 and 3 so far as they are realleged in the second cause of action.

Mr. Colin.—It is a denial only in so far as it pertains to the allegations of Paragraphs 4 and 5.

Mr. Memhard.—Now, the parties have entered into a stipulation of facts, and I think most of the facts will be stipulated—I will read from the stip- 56
ulation.

It is stipulated that prior to May 1st, 1923, the firm of Knauth, Nachod & Kuhne prepared and distributed a book—

Mr. Goldmark.—But that is not the exact wording of the stipulation.

Mr. Memhard.—Let me tell you the terms of the stipulation, your Honor. We have entered into a stipulation with the following introductory paragraph and the concluding paragraph—the rest relates to the facts which are submitted:

"For the purpose of any trial of the reclamation claim of the First National Bank of Trini- 57
dad, Colorado (hereinafter referred to as the Claimant) the following facts are stipulated to be true, and this stipulation shall be available for use by the Claimant and the Trustee subject to the provisions hereinafter contained."

Then follows a recital of the facts which are stipulated to be true.

Then it concludes with the following:

"All objections to the admission in evidence of any fact or facts hereinabove stipulated are

58 waived except objections on the ground of irrelevancy and/or immateriality."

Then, further: "Nothing in this stipulation shall be deemed to limit the right of either party hereto to offer such other and further testimony and proof herein as that party may be advised, the sole purpose of this stipulation being to avoid the necessity of producing common law evidence to prove the truth of the facts herein stipulated to be true."

Now I am proceeding to offer, on the record, the facts stipulated to be true in the order in which they appear.

59 It is stipulated that prior to May 1st, 1923, the firm of Knauth, Nachod & Kuhne (hereinafter referred to as the bankrupts) prepared and distributed a book known as "List of Foreign Correspondents" among various firms and institutions throughout the United States, including the Claimant; that the copy of the list of foreign correspondents which I hold in my hand is a copy of the said list of foreign correspondents and the provisions of it were in full force and effect—

Mr. Goldmark.—I submit you must offer precisely what I stipulated.

Mr. Memhard.—You stipulated that these facts are true.

60 Mr. Goldmark.—But I don't know whether you are summing up or what you are doing. You have not offered the paragraph which I conceded to be a fact.

Mr. Memhard.—If you will permit me to conclude, you will see what I am offering.

Mr. Goldmark.—You are stating language in the record which is not in the stipulation.

The Master.—I think you had better stick to the stipulation.

Mr. Goldmark.—At this particular point it is

not of great materiality, but we may as well understand what we are doing. 61

Mr. Memhard.—I think if you will let me conclude my statement as to the first paragraph, you will see that there is no difference between us.

Mr. Goldmark.—I will stand on my objection.

The Master.—Sustained, you will have to read the exact stipulation.

Mr. Goldmark.—I ask to have this last part stricken from the record.

The Master.—Yes, strike it out.

Mr. Memhard.—Very well, I will read from the stipulation.

(Reading). Prior to May 1st, 1923, the firm of Knauth, Nachod & Kuhne (hereafter in this stipulation referred to as the bankrupts) prepared and distributed a book known as "List of Foreign Correspondents" among various firms and institutions throughout the United States, including the Claimant. A copy of the said book received by the Claimant has been initialed by the attorneys for the Trustee and the attorneys for the Claimant and constitutes Exhibit 1 hereof. 62

I offer it in evidence.

(Received in evidence and marked Claimant's Exhibit No. 1, October 24th, 1924.)

Mr. Memhard (Continuing reading)—The provisions of said Exhibit 1 were in full force and effect on May 19th, 1923, and so continued until the filing of the petition in bankruptcy herein on or about June 16th, 1923. 63

Now, if your Honor please, I would like to read briefly from some portions of this exhibit because I think they will help your Honor in passing upon the admissibility.

Mr. Goldmark.—I understand that you have now offered in evidence Paragraph 1 of the stipula-

64 tion, plus the exhibit which you have offered in evidence.

Mr. Memhard.—That is correct.

(Mr. Memhard then read from Claimant's Exhibit 1.)

Mr. Memhard.—The portions which I read are referred to as follows: Page 1, first and second paragraphs beginning with "Foreign Exchange to our correspondents," and so forth; page 2, the captions, "Terms and Conditions Governing the use of K. N. & K. Drawing Service," and the two paragraphs following, the two paragraphs of section numbered one; page 3, Section 7; page 4, section 12; page 4, section 13, the first sentence;
65 page 8, section 21, the first sentence; page 13, the caption, "List of Foreign Correspondents" and the next sentence reading, "drawings under our protection must be confined to the following banks."

Mr. Goldmark.—For the sake of clarity, may I call attention to the fact that some of those provisions refer specifically to money orders? I just merely call attention to that fact without arguing its effect.

Mr. Memhard.—Would you care to point out which paragraph?

Mr. Goldmark.—At the top of page 6.

Mr. Colin.—Between pages 6 and 10 the para-
66 graphs refer to money orders and thereafter to cable transfers.

Mr. Memhard.—It is stipulated that prior to May 19th, 1923, the bankrupts prepared and distributed among various firms and institutions throughout the United States, including the Claimant, bound volumes entitled "Foreign Drafts" to be used by such distributees in drawing drafts under and subject to the terms and conditions specified in such volumes entitled "Foreign

Drafts" and in volumes like Exhibit 1 hereof, 67
which is in evidence.

One of said volumes of "Foreign Drafts" received by the Claimant from the bankrupts, and including drafts numbered 61,151 to 61,200 has been initialed by the attorneys for the Trustee and the attorneys for the Claimant and constitutes Exhibit No. 2 hereof, and I offer it in evidence.

(Received in evidence and marked Claimant's Exhibit No. 2, October 24th, 1924.)

Mr. Memhard.—Now I am reading from Exhibit No. 2, the following:

"Foreign Drafts. 68

"The terms and conditions under which our correspondents may use the within forms are contained in our list of foreign correspondents (that is Exhibit No. 1 in evidence) and are subject to change by us from time to time."

Now I will read from the first paragraph: "Upon receipt of advice of draft accompanied by adequate funds payable at par in New Yark, we shall promptly forward our advice of same, and make provision for its payment abroad, provided it is drawn on a bank named in our latest list of correspondents."

Now I will read from the second paragraph: 69
"Under this arrangement our correspondents draw drafts for their own account as principals and our name does not appear, our sole function being to advise the drawees of the issue of drafts drawn by our correspondents and to provide for payment, in which function we act as agents of the drawers."

Now I shall read from the fourth paragraph:

"Further information and instructions are contained in our latest list of foreign correspondents

70 (Exhibit No. 1 in evidence) the provisions of which are hereby referred to and made a part hereof. The use of our facilities will be considered as acceptance of our conditions."

It is stipulated that on May 19, 1923, pursuant and subject to the provisions contained in Exhibits 1 and 2 hereof, which are in evidence, the bankrupts notified the Claimant that the rate for 24,360 Italian Lira on that day would be .0489 per Lire. In fixing the aforesaid rate the bankrupts fixed an amount which was estimated by them to be sufficient to leave them a profit in the transaction.

It is stipulated that pursuant and subject to
71 the provisions contained in Exhibits 1 and 2 and on May 19, 1923, Claimant drew a draft, copy of which is hereto annexed and marked Exhibit 3 hereof.

I offer the draft in evidence, to be marked Exhibit No. 3.

(The draft referred to was received in evidence and marked Claimant's Exhibit No. 3 of October 24, 1924).

Mr. Memhard.—I call your Honor's attention to the fact that that is a draft from Exhibit 2 in evidence as you will note by referring to the Exhibit.

72 It is stipulated that pursuant and subject to the provisions of Exhibits 1 and 2 in evidence, and on May 19, 1923, the Claimant remitted to the bankrupts an "advice," which was one of the forms contained in Exhibit 2 hereof, which is in evidence, a copy of which I hold in my hand and which I offer in evidence as Exhibit No. 4.

(Received in evidence and marked Claimant's Exhibit No. 4 of October 24, 1924).

Mr. Memhard.—With said Exhibit 4, the Claim- 73
ant sent to the bankrupts $1,191.21, which was included in Claimant's check for $3,518.95, a copy of which I hold in hand and which it has been stipulated would be marked Exhibit No. 5—I offer it in evidence.

(Received in evidence and marked Claimant's Exhibit No. 5 of October 24, 1924).

Mr. Memhard.—And which included moneys sent in connection with other advices of the same character.

I call your Honor's attention to the fact that
that is a copy of the form of advice included in 74
Exhibit 2 in evidence.

It is stipulated that the advice and the check, of which Exhibits 4 and 5 in evidence are copies, were received by the bankrupts on May 22, 1923, and receipt thereof was acknowledged to the Claimant. Said check was duly deposited by the bankrupts in their general checking account in the Guaranty Trust Company of New York on May 22, 1923, and the bankrupts received credit for the amount thereof with the Guaranty Trust Company on that date.

It is stipulated that on or about May 22, 1923,
the bankrupts mailed to the Banca Commerciale 75
Italiana at its Genoa office six papers which constituted a document known as "S S 8469-B." The papers which I hold in my hand are copies of the six papers and I offer them in evidence to be marked Exhibits Nos. 6, 6-A, 6-B, 6-C, 6-D and 6-E.

(Received in evidence and marked Claimant's Exhibit Nos. 6, 6-A, 6-B, 6-C, 6-D and 6-E of October 24, 1924).

76 Mr. Memhard.—And that at the same time there was mailed to the Banca Commerciale Italiana at its Sassari branch a duplicate of the paper copy of which is in evidence and is marked Exhibit 6-D. These papers were received by the Banca Commerciale Italiana on or before June 4, 1923.

Now it may aid your Honor, with the approval of the other side, to call attention to some of the mechanics of that. They are all part of the same document which has been described as SS 8469-B— the bankrupts call that, I think, the Steamer Block. Exhibit 6, you will note, is a summary or list of the totals of the figures appearing on

77 each of the following Exhibits.

You will notice that Exhibit 6 has the total 197,508.60 and that it is made up of the totals which appear in the following Exhibits, 6-A to 6-E; and the copy of 6-D, which was mailed to the Sassari branch of the Banca Commerciale Italiana, includes draft No. 61,161 drawn by the First National Bank of Trinidad, Colorado, dated May 19th, for 24,360 Lire in favor of Zara Sanna Giovanni, and that the draft to which I call attention is the draft in suit.

Now will your Honor note that these papers are a direction by the bankrupts to the Banca Commerciale Italiana to "Protect to the debit of

78 our account" the draft set forth, and to "Charge the same to the bankrupts' account."

Mr. Goldmark.—If you are going to do that, you may as well call attention to the bottom of Exhibit 6-D, which relates to the same draft.

The Master.—That says "Please honor the above list of drafts," and so forth.

Mr. Memhard.—Well, you may have that on the record.

It is stipulated that the Banca Commerciale Italiana sent to the bankrupts through the mail,

and the bankrupts or the receiver received on or about June 16, 1923, June 25, 1923, and July 5, 1923, respectively, the papers which I hold in my hand and which I offer in evidence to be marked Exhibit Nos. 7, 8 and 9. 79

Mr. Goldmark.—To those papers I object on the ground that they are irrelevant and immaterial—our advices from the Banca Commerciale Italiana to the bankrupts are irrelevant and immaterial. We shall be glad to have counsel, for the aid of the Court and myself, point out in what way he deems communications which we received from the Banca Commerciale Italiana with respect to fixing any rights of the Claimant relevant.

Mr. Memhard.—The trustee stipulates, later, that this method of dealing, of sending statements and of charging the account was approved. 80

Mr. Goldmark.—I stipulated nothing so far as direction is concerned, except what is already in evidence.

Mr. Memhard.—I think the Exhibit should be admitted in evidence. Let me read the rest of the stipulation.

Mr. Goldmark.—Is the offer now withdrawn temporarily or is he offering a further stipulation, or what?

The Master.—I suppose it is still pending.

Mr. Memhard.—Let me conclude the stipulation, if you will— 81

And that statements of the type of Exhibits 7, 8 and 9 were sent by Banca Commerciale Italiana to the bankrupts approximately each week.

Mr. Goldmark.—I object to that for the same reason.

Mr. Memhard.—Won't you let me finish that paragraph?

The Master.—Let him finish the paragraph.

Mr. Memhard.—The practice of Banca Commerciale Italiana in debiting the bankrupts with the

82 amounts of drafts advised, as shown on these statements, was recognized as proper by the bankrupts.

Now I offer these papers in evidence to be marked Exhibits Nos. 7, 8 and 9.

Mr. Goldmark.—I press my objection that they are irrelevant and immaterial and inadmissible. There is nothing here to show that they have any relevancy to the issues which is being tried between the Claimant and the bankrupts or its trustee.

The Master.—But there is a further stipulation to the effect that this practice was recognized by the bankrupts as proper.

83 Mr. Goldmark.—I don't see the relevancy of that as between the Claimant and the bankrupts. If he indicates what the relevancy is, we may get somewhere, but I do not see the relevancy between the Claimant and the bankrupt.

Mr. Memhard.—Well, Exhibit 8 shows the reference to the Steamer Block S S 8469 B, 197,508.60 Lire, which is already in evidence and which is the amount which included the amount of the draft of the Claimant drawn on that bank, and this shows that the bankrupt, in furtherance of its service, advised the foreign bank, as it said it would do, and provided the money as it said it

84 would do.

Mr. Goldmark.—This doesn't show that. I let the advices go into evidence without objection, but this is not the advice that you are offering.

Mr. Memhard.—And it shows that the bank debited the account of Knauth, Nachod & Kuhne with that total, which included the draft in suit.

One of the questions in the case is whether there was an equitable assignment abroad, and this shows how they regarded their relations and what they did in furtherance of them, and the three

statements cover the period which connect up the totals, with the ultimate transfer of the balance to the trustee. 85

The Master.—I am wondering how that can affect the arrangement between Knauth, Nachod & Kuhne and the Claimant, what the bank in Italy did.

Mr. Memhard.—Because the bankrupt undertook to do certain things and we claim an equitable assignment of the funds abroad, and that statement shows that they debited the account of the bankrupts and credited something else, and we rely upon that to show what the bankrupts did in furtherance of its agreement with the Claimant. Without that, we cannot show what they did 86
in furtherance, and we must show that the money came back into the hands of the trustee. Without that we shall be unable to show that that money came back to the trustee.

The Master.—I will admit them for the present and I will hear further argument as to whether they should be stricken out.

Mr. Goldmark.—I respectfully except.

(Received in evidence and marked Claimant's Exhibits Nos 7, 8 and 9 of October 24, 1924).

Mr. Memhard.—I would like to call your 87
Honor's attention, with relation to these exhibits, to the fact that they show that in carrying the account of the bankrupts from week to week, the amount of drafts advised abroad were charged against the account as soon as the Banca Commerciale Italiana received advice of the draft and without waiting for the draft to be presented or paid, and also that Exhibit 9, which is a statement covering the period up to the date of the filing

88 of the petition in bankruptcy, shows that at no time prior to the bankruptcy was the amount of S. S. Steamer Block 8469 B, credited back to the account of the bankrupts.

The Master.—This Exhibit 9, is that 15th of June?

Mr. Memhard.—Up to the 16th of June, that is the date of bankruptcy.

The Master.—I don't know whether that is fifteen or sixteen.

Mr. Memhard.—I think it will be conceded that that is the 16th.

Mr. Colin.—It is conceded that it is the 16th.

89 Mr. Memhard.—I would like to have it noted on the record that what immediately follows relates to paragraph 9 of the stipulation.

It is stipulated that when the Banca Commerciale Italiana at Genoa, received the papers in the form of Exhibits 6 to 6-E in evidence, said Banca Commerciale Italiana thereon debited an account which the bankrupts maintained with said bank at its Genoa office to the extent of the aggregate amount of the drafts referred to in Exhibit 6 in evidence, and simultaneously credited on its books an account termed "Drafts Payable," in which account were also credited amounts of drafts advised to the said Banca Com-

90 merciale Italiana for the payment by other depositors or clients of the Banca Commerciale Italiana in addition to the bankrupts.

Mr. Goldmark.—If your Honor please, in view of your ruling with regard to Exhibits Nos. 7, 8 and 9, I do not object to that statement but I reserve the right to move to strike it out in the event that you subsequently determine to strike out the exhibits.

The Master.—You do object to it, is that what you mean?

Mr. Memhard.—Let me conclude my statement. 91
Mr. Goldmark.—To make myself perfectly clear, what I mean is that in the present state of the record I am not objecting to it, but in the event that you strike out those other exhibits, then this testimony may also become incompetent.

Mr. Memhard.—Let me finish my sentence.

The Master.—Finish your paragraph and I will see.

Mr. Memhard.—I would like to have this on the record in complete sequence, I would like to read it again.

It is stipulated that when the Banca Commerciale Italiana at Genoa received the papers in the form of Exhibits 6 to 6-E in evidence, said 92
Banca Commerciale Italiana thereupon debited an account which the bankrupts maintained with the bank at its Genoa office to the extent of the aggregate amount of the drafts referred to in Exhibit 6 in evidence, and simultaneously credited on its books, an account termed, "Drafts Payable," in which account were also credited amounts of drafts advised to the said Banca Commerciale Italiana for payment by other depositors or clients of the Banca Commerciale Italiana in addition to the bankrupts. Interest was allowed to the bankrupts on the amount of the balance standing to their general credit, but no interest was allowed to the bankrupts or to anyone else upon 93
the amount credited to the account termed, "Drafts Payable," as a result of advices from the bankrupts. The Banca Commerciale Italiana received no compensation or commission for their services in honoring drafts drawn upon them by the bankrupts, or by their correspondents pursuant and subject to the provisions of Exhibits 1 and 2 in evidence, except such compensation if any, as was measured by the use, without the payment of interest thereon, by said Banca Com-

94 merciale Italiana, of the funds standing to the credit of the account termed "Drafts Payable."

Mr. Goldmark.—Now may I repeat my statement that, in the present state of the record, I do not object to paragraph 9 of the stipulation which has just been read by counsel, but I do reserve the right, in the event that you strike out Exhibits Nos. 7, 8 and 9, to move to strike it out.

Mr. Memhard.—If your Honor please, this paragraph, as stipulated, has nothing whatever to do with the other. This is stipulated to be true, stipulated as a fact.

Mr. Goldmark.—I am talking about the materiality. I think I have made myself clear.

95 The Master.—That motion may be reserved.

Mr. Memhard.—Please note on the record that what I am reading now refers to paragarph 12, of the stipulation:

It is stipulated that on June 16th, 1923, the Receiver herein sent a cablegram to the Banca Commerciale Italiana at Genoa, Italy, copy of which I hold in my hand and offer in evidence as Exhibit No. 10.

(Received in evidence and marked Claimant's Exhibit No. 10, October 24, 1924).

96 Mr. Memhard.—Please note on the record that what I am reading now refers to paragraph 13 of the stipulation:

It is stipulated that on July 5, 1923, the Receiver received from Banca Commerciale Italiana, a letter dated June 22, 1923, together with enclosures therein referred to, and that Exhibit No. 9 in evidence was one of the enclosures and the paper I have in my hand is a copy of the letter itself, which I offer in evidence as Exhibit No. 11.

Mr. Goldmark.—I make the same objection to 97
that.

(Received in evidence and marked Claimant's Exhibit No. 11, October 24, 1924).

Mr. Memhard.—This exhibit shows that in arriving at the balance in the bankrupts' favor, the net amount, after deducting from the general balance, the amount of all drafts advised, was taken. This amount is arrived at on Exhibit 9 to which I referred, after deducting all drafts advised.

Now I would like to read the last paragraph on the second page of the letter, Exhibit 11, in evidence: 98

"We enclose herewith a statement of the account of Messrs. Knauth, Nachod & Kuhne as at the close of business on the 16th inst. (That is June 16th) showing, in principal only, a balance in their favor of:

Lit. 89. 351,26=from which is to be deducted an approximate sum of:

Lit. 8. 954,00=debit balance Dollars Account. ($407.15) leaving a balance of:

Lit. 78. 397,26.

With reference to Exhibit 9, your Honor will note that this balance is arrived at by deducting the drafts advised to the bank, and I would like 99
to read from page 2 of the letter Exhibit 11, the following:

"During the last few days several drafts already debited in account have been presented, the payment of which we have refused, and would ask you to inform us by cable whether we are to pay drafts which have already been passed to the debit of the account or whether we are to consider them as cancelled and re-credit them to the account of Messrs. Knauth, Nachod & Kuhne."

100 I would also like to read the following paragraph from page 2 of Exhibit 11 in evidence:

"We would ask you further to note that the following orders are being held in abeyance, not having been debited to the account through lack of funds."

Then follows a list of orders aggregating several hundred thousand Lire.

I would like to point out that that apparently indicates that when they didn't have a balance, they did not credit the drafts payable account.

I would like to have it noted on the record that what I am reading now refers to paragraph 14 of the stipulation:

101 It is stipulated that the following Cablegrams and letters passed between the receiver and the Banca Commerciale Italiana;

Cablegram June 26, 1923, the receiver to Banca Commerciale Italiana;

Cablegram received June 30, 1923, Banca Commerciale Italiana to the receiver;

Letter June 29, 1923, receiver to Banca Commerciale Italiana;

Letter July 12, 1923, Banca Commerciale Italiana to receiver;

Cablegram received July 13, 1923, Banca Commerciale Italiana to receiver;

102 Cablegram July 13, 1923, receiver to Banca Commerciale Italiana;

Cablegram August 23, 1923, receiver to Banca Commerciale Italiana.

Photostatic copies of the aforesaid letters and cablegrams are hereto annexed and marked Exhibits 12, 13, 14, 15, 16, 17 and 18 respectively.

(Cablegram June 26, 1923, receiver to Banca Commerciale Italiana received in evidence and marked Claimant's Exhibit No. 12 of October 24, 1924).

(Letter June 29, 1923, receiver to Banca Commerciale Italiana received in evidence and marked Claimant's Exhibit No. 14 of October 24, 1924). 103

(Cablegram received June 30, 1923, Banca Commerciale Italiana to receiver, received in evidence and marked Claimant's Exhibit No. 13 of October 24, 1924).

(Letter of July 12, 1923, Banca Commerciale Italiana to receiver, received in evidence and marked Claimant's Exhibit No. 15 of October 24, 1924).

(Cablegram received July 13, 1923, Banca Commerciale Italiana to receiver, received in evidence and marked Claimant's Exhibit No. 16 of October 24, 1924). 104

(Cablegram July 13, 1923, receiver to Banca Commerciale Italiana, received in evidence and marked Claimant's Exhibit No. 17 of October 24, 1924).

(Cablegram of August 23, 1923, receiver to Banca Commerciale Italiana, received in evidence and marked Claimant's Exhibit No. 18 of October 24, 1924).

Mr. Memhard.—Referring to Exhibit 14, permit me to call your Honor's attention to the last paragraph of this letter, in which the receiver directs Banca Commerciale Italiana to rule off the account of the bankrupts on the day Banca Commerciale Italiana got a cable of June 16th, which is Exhibit 10. It reads as follows: 105

"I request you to kindly rule off the account of Knauth, Nachod & Kuhne on the day on which my first cable (confirmation enclosed) informing you of the receivership reached you, and to forward to me by return mail a statement of their account up to that date, as well as a list of all unexecuted cable transfers and unpaid drafts and

106 money orders, stating the numbers of reports in which items were advised by Knauth, Nachod & Kuhne."

Referring to Exhibit 15, beginning the last paragraph, I read from the bottom of page one:

"We would further refer you to our letter of June 22nd, in which we desired you to advise us by cable whether we are to pay drafts which have already been passed to the debit of the account or whether we are to consider them as cancelled and to re-credit to the account of Messrs. K. N. & K."

Let me read Exhibit 17 (Counsel reads same).

And I would like to have the record note that
107 what I am reading now refers to paragraph 15 of the stipulation:

It is stipulated that on September 26, 1923, the Receiver received from the Banca Commerciale Italiana, a letter dated September 10, 1923, together with enclosures, copy of which letter and enclosures are annexed hereto and marked Exhibits Nos. 19, 19-A and 19-B, respectively, and I offer them in evidence.

(Received in evidence and marked respectively Claimant's Exhibits Nos. 19, 19-A and 19-B).

Mr. Memhard.—Referring to Exhibit 19, I
108 should like to read the second paragraph of that letter of September 10th, reading as follows:

"Information has now been received from all our branches regarding unpaid drafts and we enclose herewith statement of drafts which had been debited but not paid prior to the appointment of the Receivership."

Now with regard to Exhibit 19-A, which is the list of unpaid drafts referred to in Exhibit 19, the letter of September 10th, I would like to call

attention to the fact that the draft in suit is specified in that list; that is, draft No. 61,161, which is Exhibit 3 in evidence, drawn by the First National Bank of Trinidad, Colorado, on, as they say, "Our Sassari Office," for Italian Lire 24,360. 109

Now I would like to point out that the total of all the drafts charged and unpaid, as shown on the statement enclosed, being Exhibit 19-A, including the draft in suit, was 1,526,048.48 Lire, which corresponds with the amount shown in the letter, Exhibit 19, and in the statement of account, Exhibit 19-B, as having been recredited to the account of the bankrupts; and also that in the statement reference is made to the letter of September 10, 1923. 110

If your Honor will note on the right hand side, where that total of 1,526,048.48 Lire appears, you will see reference to the letter of September 10th.

I would also like to point out, that in the letter the Banca Commerciale Italiana advised the Receiver that it has passed telegraphic instructions to its New York Agency to pay him an amount, which as shown by the statement, Exhibit 19-B, included the amount recredited on account of all unpaid drafts, including the draft of the claimant.

Now I would like to have it noted on the record that what I am reading refers to paragraph 16 of the stipulation. 111

It is stipulated that the Receiver and/or Trustee has received from the Banca Commerciale Italiana $67,548.06, being the amount of 1,629,550 Lire, less $4,115, referred to in Exhibits 19 and 19-B, in evidence, converted into American dollars.

For the convenience of the Master I would like to point out the fact that 1,629,550 Lire is 1,629,-

112 770 less 220 Lire for cable expenses mentioned in Exhibit 19, and includes the sum of 1,526,048.48 Lire recredited to the account of the bankrupts—that appears on Exhibit 19-B.

Referring to Exhibit 19, the total credit carried forward on Exhibit 19-B, is the total credit carried forward from Exhibit 9, namely, 51,825,703.14 Lire, and that the debit total carried forward to Exhibit 19-B is 51,738,351.88, which is the total of debits on Exhibit 9, namely, 51,825,703.14, less the amount brought down as a credit balance, namely, 87,351.26 Lire. That will help your Honor connect up those statements.

113 Now I would like to have it noted on the record that what I am reading refers to paragraph 17 of the stipulation:

It is stipulated that the aforesaid draft, Exhibit 3 in evidence, was duly presented for payment and payment thereof was refused and notice thereof duly given to the Receiver and to the Trustee. The draft still remains unpaid.

Mr. Trosk.—I think the record ought to show that the original draft is in the possession of the claimant and is ready to be surrendered or delivered up to the Trustee.

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114 Hearing adjourned to October 24, 1924, at 2:00 P. M.

UNITED STATES DISTRICT COURT, 115

SOUTHERN DISTRICT OF NEW YORK,

In Bankruptcy.

Before ROBERT P. STEPHENSON, ESQ., Special Master.

In the Matter
*of*
KNAUTH, NACHOD & KUHNE,
Bankrupts. 116

32 BROADWAY, NEW YORK CITY,
October 24th, 1924; 2.00 P. M.

HEARING ON RECLAMATION OF FIRST NATIONAL BANK OF TRINIDAD, COLORADO.

Proceeded pursuant to adjournment.

MESSRS. ROSENBERG & BALL, Attorneys for Trustee.
BY GODFREY GOLDMARK, ESQ., GEORGE G. ERNST, ESQ., and RALPH F. COLIN, ESQ., Of Counsel. 117
MESSRS. O'BRIEN, BOARDMAN, PARKER & FOX, Attorneys for Claimant.
BY GEORGE TROSK, ESQ., and WILLIAM DE-FOREST MANICE, ESQ., Of Counsel.
ALLEN R. MEMHARD, ESQ., Of Counsel for Claimant.

Mr. Memhard.—I would like to state, with reference to some objections made when I read the

stipulation into the record in language slightly different from the written stipulation, that I was seeking to avoid the use of the words, "Hereto Annexed," by saying, "Which I hold in my hand," because the words, "Hereto Annexed," had no meaning.

Now I hold the original of draft 61,161 and offer to surrender it up to the Trustee for whatever value or purpose the Master may attach to it.

I would like to call attention to the fact that this action is not on the draft. The draft is one by the Claimant on the Banca Commerciale Italiana
119 and has no relation to the bankrupt; the bankrupt's name nowhere appears on the draft and a copy of it is already in evidence.

Now I would like to call Mr. Schulze.

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Otto H. Schulze, called as a witness on behalf of the Claimant, being duly sworn, testified as follows:

*Direct-examination by Mr. Memhard:*

Q. Will you give your address, Mr. Schulze? A. 74 Broadway.

120 Q. You are employed by the Trustee in Bankruptcy of Knauth, Nachod & Kuhne? A. I am.

Q. And prior to that employment you were employed by the receiver? A. Yes.

Q. And prior to that employment you were employed by the bankrupts? A. I was.

Q. For how long? A. From May, 1920.

Q. To the date of bankruptcy? A. Yes, sir.

Q. In what capacity were you employed by the bankrupts? A. General auditor.

Q. And in that connection you had access to all the books and records of the bankrupt? A. I did.

Q. And audited all of its transactions as shown by the books? A. Yes, sir.

Q. Did you have to do with the auditing or examining of any transactions other than those shown in the books? A. Well, my work consisted of other work than auditing—I don't know how to answer your question.

Q. As far as your duties as auditor were concerned? A. Well, it may go back further than just auditing records. I was in charge of the various departments, to see that they functioned properly, in order that their records might tie in with the general records. 122

Q. That was part of your duty? A. Yes, sir.

Q. And since your employment by the receiver and trustee you have had the same access to all the books and records that you had prior to the bankruptcy? A. I have, yes, sir.

Q. Can you produce any book or record, other than the office copy of Steamer Block number 8469-B, which contains reference, by name and date and amount of drafts, to the draft in suit here, that is, the one drawn by the Trinidad Bank of Colorado, the Claimant, No. 61,161. Is that clear? A. I don't think it is quite clear. You mean showing the name and number—will you just read the question? 123

Q (Read)? A. No.

Q. And you cannot produce any such record because you have no such record, is that so? A. That is so.

Q. After the bankrupt received, from the Claimant here—you understand the Claimant is the Trinidad Bank? A. Yes, sir.

124 *Otto H. Schulze for Claimant—Direct.*

Q. The dollar equivalent of the twenty-four thousand three hundred and sixty Lire, did the bankrupt carry on its books of account, as a liability, the money it received from the Trinidad Bank?

Mr. Goldmark.—I object to that as calling for a conclusion. He may show what the books showed.

The Master.—Sustained.

Mr. Memhard.—He testified that he was an auditor and employed as such for a number of years and had charge of all the
125 records of account of the bankrupt, and I submit he is qualified as an expert to answer that question.

Mr. Goldmark.—It is not a question of expert testimony, it is a question of law.

The Master.—You asked him what the books showed—that is secondary evidence.

Q. Is there any book which contains an account with the First National Bank of Trinidad, Colorado, or any reference to the First National Bank of Trinidad, Colorado, other than the office copy of the Steamer Block? A. Yes, there is a record.

Q. What is it? A. It is a record for what we
126 call a bill ledger, in which record—you want me to explain?

The Master.—No, you have answered the question.

Q. Is that the only record? A. That is the only record.

Q. Will you produce that book? A. I haven't it right here.

Q. Is there any book in which the bankrupt carried as a liability, the amount of money received

from the First National Bank of Trinidad, Colorado, in connection with this draft No. 61,161?

Mr. Goldmark.—I make the same objection to that and add to it the objection that the use of the term "book" nowadays is a very indefinite one.

Mr. Memhard.—Well, book or record.

Mr. Goldmark.—I make the same objection.

The Master.—I sustain the objection.

Mr. Memhard.—I ask to have an exception to the ruling and to the preceding one. 128

The Master.—Exception noted.

Q. The other record you describe as a bill ledger record? A. Yes, sir.

Q. Was that a record in which you kept a record of differences or minor adjustments which were to be made between the bankrupt and a drawer under the drawing service, Exhibit No. 1? A. That is true.

Q. It had no other function than merely that it contained a record of such minor adjustments as sometimes arose in connection with the transaction? A. That is right.

Q. The bankrupt carried, on its books, an account with the Banca Commerciale Italiana, Genoa, Italy? A. Yes, sir. 129

Q. Were entries made in that account of the amounts of Lire mentioned in Steamer Block letters? A. Yes, sir.

Q. And those entries charged or credited the Banca Commerciale Italiana with the amounts of the Steamer Block letters? A. Yes, sir.

Q. Which was it? A. Credited.

Q. Did the bankrupt, after crediting the Banca

130 *Otto H. Schulze for Claimant—Direct.*

Commerciale Italiana with the amounts of Lire advised in Steamer Block letters, thereafter ever treat the amounts of such lire as an asset?

Mr. Goldmark.—I object to that as calling for a conclusion.

Mr. Memhard.—On their books.

The Master.—What is the objection?

Mr. Goldmark.—If they ever treat it as an asset—I don't know what he means.

Mr. Memhard.—I said on their books. It is perfectly obvious that we must allow
131 some recognition of these terms in connection with bookkeeping and financial transactions, otherwise we get nowhere.

The Master.—Do you object on the ground the books are not here?

Mr. Goldmark.—No. I don't object on the ground the books are not here.

The Master.—You have no objection to this witness testifying to what the books show without their being present?

Mr. Goldmark.—No.

The Master.—Then I will overrule the objection.

132 Mr. Goldmark.—Exception.

Q. (Read as follows): Did the bankrupt, after crediting the Banca Commerciale Italiana with the amounts of Lire advised in Steamer Block letters, thereafter ever treat the amounts of such Lire as an asset on their books? A. No.

Q. What became of the money which was received by the bankrupts from the First National Bank of Trinidad, Colorado?

Mr. Memhard.—I will withdraw that question.

Q. Upon receipt from the First National Bank of Trinidad, Colorado, of the check which is Claimant's Exhibit No. 5 in evidence, for $3,518.95, was that check deposited in one of the bank accounts of the bankrupt? A. According to this Exhibit 5, it was deposited in the Guaranty Trust Company.

Q. Was the First National Bank of Trinidad, Colorado, credited, anywhere, in any book or record with that amount of money? A. No.

Q. Was any record set up in the bankrupt's books, or an entry made showing an indebtedness by the bankrupt of that amount of money to the 134
First National Bank of Trinidad, Colorado?

Mr. Goldmark.—That is the same question I objected to before.

The Master.—Showing a liability?

Mr. Goldmark.—He now uses the word "Indebtedness"; I don't know that there is any distinction.

Mr. Memhard.—I submit that some latitude must be allowed with regard to the meaning of terms everyone understands.

The Master.—Why not ask him what the books show?

135

Mr. Memhard.—I am trying to get at it. You appreciate that this man is in the bankrupt's employ, or rather in the trustee's employ.

The Master.—Oh, yes.

Mr. Goldmark.—He has already shown what the books show; that is, he has shown it in part, perhaps, but now he is trying to go beyond that.

Mr. Memhard.—If we should bring here

136 *Otto H. Schulze for Claimant—Direct.*

all the books and records, that would be one thing. But we could simplify this a great deal by asking this man some simple questions because he is a competent expert in their employ.

The Master.—Let me hear the question.

Q. (Read).

The Master.—I sustain the objection.

Mr. Memhard.—I respectfully except.

Q. Now the bankrupt was indebted to various
137 persons, was it not, during this period from May 19th to the date of bankruptcy? A. It was.

Q. And wasn't that indebtedness set up as a liability on the books of the bankrupt? A. No, not all of it.

Q. Did the books of the bankrupt contain accounts with persons to whom it was indebted? A. It did.

Q. And that indebtedness was a liability, was it not? A. Yes.

Q. And did not the books of the bankrupt show, either in detail or in the aggregate, all of its liabilities?

138 Mr. Goldmark.—I object to that as calling for a conclusion. I don't see how this man can pass on the question of whether or not the books showed liabilities of the bankrupt.

The Master.—He may be able to tell, I will overrule the objection.

A. I can't answer that question.

Q. Well you were the auditor, were you not? A. Yes.

Q. And the books were kept under your direction, were they not? A. Yes.

Q. And they were supposed to have been kept correctly? A. Yes.

Q. It was your duty to know that they were kept correctly, was it not? A. Yes.

Q. Then why can't you answer the question? A. Well, there were various suits pending against Knauth, Nachod & Kuhne that were not set up on the books as liabilities and afterwards turned out to be liabilities.

Q. You refer in general to unliquidated liabilities or obligations? A. Yes. 140

Q. But as to all definitely known transactions and liabilities, were they all reflected in the books and records? A. They were reflected on the records with the exception of when it was made out in balance sheet form, then net positions were taken and the liabilities were not shown or were the assets shown, in such transactions.

Q. But no cash ever came into the business that was not shown on the books? A. No, sir.

Q. And those balance sheets showed aggregate liabilities did they not? A. Aggregate net liabilities and net assets.

Q. After May 19, 1923, were the balance sheets taken off from the books of the bankrupt? A. 141 Yes, sir.

Q. On what date? A. May 31st—that is, at the end of May, 1923.

Q. And when subsequently? A. Then one as of June 15th, the date of bankruptcy.

Q. Referring to the Steamer Block, Exhibit 6 to 6-E, you will note, with reference particularly to Exhibit 6-D, the amount of the draft drawn by the claimant here, of 24,360 Lire? A. Yes.

Q. And I will tell you that it has been stipu-

lated here that the money to cover that draft was $1,191.21, and that that $1,191.21 was included in the check for $3,518.95.

Q. What was the date on which the bankrupt received advices from the Banca Commerciale Italiana that that Steamer Block had been received? A. What is the date?

Q. The bankrupt received advices from the Banca Commerciale Italiana from time to time acknowledging receipt of Steamer Blocks? A. Yes.

Q. And in the statements which the bankrupt
143 received from the Banca Commerciale Italiana it showed debit items corresponding to the amounts of the Steamer Blocks? A. Yes.

Q. Now you will note there, by reference to Exhibit 8, that the amount of this Steamer Block, 197,508.60 Lire was charged on June 4th—do you see that? A. Yes, sir.

Q. That indicates to you, does it not, that on May 30th the Banca Commerciale Italiana had not received that Steamer Block? A. I don't know, I can't tell that.

Q. I mean if they charged it on June 4th, they evidently had not received it on May 30th. A. I don't know.

144 Mr. Goldmark.—That is purely speculative.

Q. I asked if it indicated that? A. You have the dates so close that I really can't tell.

Q. Well what was the date of the Steamer Block? A. Somewheres around the 19th, I am not sure.

Q. I will tell you that it was May 22nd? A. May 22nd, yes, sir.

Q. And what appears from Exhibit 8 there to

be the date on which the Banca Commerciale Italiana charged that amount as shown in the Steamer Block? A. June 4th, value-dated June 2nd; in other words, they made the entry on June 4th, but charged us as of June 2nd.

Q. Now the bankrupt you said prepared a trial balance as of May 30th? A. Yes, sir.

Q. And that trial balance included the net assets and net liabilities of the bankrupt on that date? A. Yes, sir.

Q. That trial balance was prepared from the books of the bankrupt? A. Yes, sir.

Q. Did that trial balance include, as a liability, 146
the amount of money which had been paid to the bankrupt by the First National Bank of Trinidad for this draft in suit?

Mr. Goldmark.—Objected to as incompetent, irrelevant and immaterial and in addition, not binding on the trustee.

The Master.—Sustained.

Mr. Memhard.—Of course, the trustee stands in the same position as the bankrupt here.

The Master.—Yes, but evidence which is admissible against the bankrupt is not necessarily admissible against the trustee. 147

Mr. Memhard.—But the rights of the parties are being determined, in part, by the records of the bankrupt which are now in possession of the trustee and I am showing what the records were at the time, and this man was the auditor at the time this transaction occurred.

The Master.—These records are only admissible against the parties to the proceeding. If Knauth, Nachod & Kuhne were a

party to the proceeding, that would be admissible. The trustee is a party to the proceeding and they are not his records.

Mr. Memhard.—Excepting that, in line with the position that your Honor indicates, we are attempting to show the relationship which existed between the Claimant and the bankrupt, Knauth, Nachod & Kuhne, and we must show, by their records, what took place after the receipt, by the bankrupt, of the money which we paid to the bankrupt for a particular purpose. Now
149 our petition alleges that it was an equitable assignment in favor of the Claimant in a fund abroad and it is material, in that connection, to show that the bankrupt, after the receipt of this money from the Claimant and the advice of it abroad and the debiting of the account of the bankrupt with the foreign bank, the Banca Commerciale Italiana, never thereafter treated that money as a liability to the drawer, the First National Bank of Trinidad, or never treated the money advised abroad as an asset of its own.

150 I submit that I must show that from the bankrupt's books and, unless I can show that, I am excluded from proving my case because my case rests largely on that record.

Mr. Goldmark.—On the theory that counsel advances, when I take a trial balance, having sent a check to X. Y. Z. in payment of an indebtedness and take that off from the asset side, that would constitute an

equitable assignment of my bank balance which I do not believe he contends.

Mr. Memhard.—Nothing of the kind.

The Master.—Let us not get into that argument. Of course, you must first prove that these books were accurate before you can put them in evidence.

Mr. Memhard.—I think it has been testified to that they were completely and accurately kept—he so testified.

The Master.—He did not testify that the trial balance was correct, did he?

Mr. Memhard.—I will ask him. 152

Q. Was the trial balance correct? A. It was correct as far as our records went.

Q. The trial balance you said was taken from your books? A. The trial balance was taken from the books.

Q. And your books were accurately and correctly kept under your supervision? A. Yes.

Q. Was that trial balance a true and correct trial balance or did you leave something out of it? A. No.

Q. Then it was a true and correct trial balance? A. Of the books, yes, sir. 153

Q. And the books correctly reflected your assets and liabilities, did they not? A. Well, I can't answer that.

Q. With the exception as you previously stated? A. No, not only with that exception but, as you understand, the books that we kept in New York were not the actual conditions of the books that were kept abroad.

Q. I am not talking about anything that hap-

154 *Otto H. Schulze for Claimant—Direct.*

pened outside of your books, please don't argue about it.

Mr. Goldmark.—He is entitled to make his explanation.

Q. I am asking you if the trial balance was a true and correct trial balance? A. But you also asked me if the assets and liabilities reflected thereon were the true assets and liabilities, and I can't answer that.

Q. Well so far as you know, the books were truly and correctly kept, were they not? A. Yes,
155 sir.

Q. And so far as you know that trial balance was a true and correct one according to the books? A. According to the books, yes, sir.

Q. And you were the auditor in charge of all the books and records, were you not? A. Yes, sir.

Mr. Memhard.—Now I press my former question.

The Master.—What was the question?

Q. (Read as follows).—Did that trial balance include, as a liability, the amount of money which had been paid to the bankrupt by the First Na-
156 tional Bank of Trinidad for this draft in suit?

The Master.—Do you mean to object on the ground the original trial balance is not produced?

Mr. Goldmark.—I do not.

The Master.—Then I overrule the objection.

Mr. Goldmark.—Exception.

Q. Does that trial balance include, as an asset, the amount of Lire advised to Banca Commerciale

157

Italiana in the Steamer Block in question, namely 197,508.60 Lire? A. I don't think I understand your question.

Q. We are talking about the trial balance which you said indicated your net position? A. Yes, sir.

Q. And you testified that when you advised a Steamer Block abroad you credited the Banca Commercial Italiana with the amount? A. Yes.

Q. And after that you took off a trial balance? A. Yes, sir.

Q. Now I am asking you whether that trial balance showed the amount of that Steamer Block 158
in Lire as an asset? A. No.

Q. It did not? A. No.

Q. The answer is it did not? A. It did not.

Q. Prior to the date of the receivership, did the Banca Commerciale Italiana, send to the bankrupt statements of unpaid drafts outstanding?

Mr. Goldmark.—What was the question?

Q. (Read)

Mr. Memhard.—I will withdraw the question.

Q. After bankruptcy, did the bankrupt or the 159
receiver receive from the Banca Commerciale Italiana a statement of unpaid drafts? A. Yes, sir.

Q. That list was sent by Banca Commerciale Italiana at the request of the receiver, or the trustee? A. Yes.

Q. Was it the practice of the Banca Commerciale Italiana to send such lists of unpaid drafts outstanding to the bankrupt? A. I can't answer as to whether this particular bank sent such state-

ments or not; they may have sent them on request—I am not in a position to state. I know we got them from some banks, but I am not sure whether we got them from this bank or not.

Q. Let me refer to the drawing service Exhibit No. 1 and to section 12 thereof on page 4, which reads: "Payment of drafts abroad is not usually reported to us; and we can only ascertain whether or not drafts have been presented for payment by making special inquiry of the drawee bank." That referred to this bank, did it not, the Banca Commerciale Italiana? A. I believe it did, yes.

161 Q. And you did not receive periodical statements from that bank showing unpaid drafts outstanding? A. No.

Mr. Memhard.—Now I call upon the trustee to produce a letter dated September 8, 1923, from Banca Commerciale Italiana to the trustee. This letter is also mentioned in the letter from the Banca Commerciale to the trustee or receiver, dated September 10th, which is in evidence.

Mr. Goldmark.—The trustee has, so far as counsel knows, no such letter.

162 Q. Will you refer to Exhibit 19, Mr. Schulze? A. Yes, sir.

Q. And note there reference to a letter of September 8th? A. Yes, sir.

Q. Can you produce that letter? A. Upon request of Mr. Manice, I looked for that letter in the files of Knauth, Nachod & Kuhne and the trustee, and I couldn't find any such letter.

Q. Can you say whether, in the ordinary course of business, that letter would have come to you? A. No, it would not have come to me in the ordinary course of business.

Q. To whom would it have come, in the ordinary course of business? A. It would have gone to the mail clerk and he would have analyzed it to find out to what department it might have referred and then referred it to that department.

Q. So you can't even now say to what individual in the bankrupt's organization that letter went? A. Not unless I know the contents of the letter.

Q. It is clear, is it not, that the letter relates to the request of the receiver and trustee for the transfer of all unpaid drafts?

Mr. Goldmark.—I don't think this man can pass on it any more than the Special Master can. 164

The Master.—You may try further.

Mr. Memhard.—If you refer to the letter, you will see that.

Q. This letter relates to an attempt on the part of the trustee to have brought back here to him the Lire standing to the credit of the bankrupt? A. Yes.

Q. That is clear, is it not? A. Yes, sir.

Mr. Goldmark.—I don't think you can qualify this man as an expert and I don't see the purpose of the testimony. 165

The Witness.—The letter of the 10th Exhibit 19, I am referring to here.

Q. Well look at the letter and see the reference to the letter of September 8th? A. Yes, I see that—

Q. Read it? A. (Witness reading) "We beg to confirm your letter of the 8th inst. and to acknowledge receipt of your cablegram of the 23rd ult. reading: 'Refer to

166 *Otto H. Schulze for Claimant—Direct.*

your letter of July 12th, please cancel all drafts charged but not paid before receivership and remit balance for our credit to Central Union Trust Co., New York.' "

"Information has now been received from all our branches regarding unpaid drafts and we enclose herewith statement of drafts which have been debited but not paid prior to the appointment of the receivership."

Q. Well, now, isn't it clear to your mind, as
167 one being familiar with the business of the bankrupt, that that letter relates to this correspondence between the Banca Commerciale Italiana and the receiver or trustee?

Mr. Goldmark.—I object to that as incompetent, irrelevant and immaterial.

The Master.—I overrule the objection.

A. I really can't say; I don't know what might have been in the letter of the 8th.

Q. But isn't it perfectly apparent to your mind, as a sensible man, that that has some relation to this correspondence between the receiver and the Banca Commerciale Italiana? A. Yes.

168 Mr. Goldmark.—That is assuming a fact not proven yet.

Q. Where would you look if you wanted to find that correspondence? A. I looked in the general files where all answered letters would be and I went to the various departments who may have had the letter from the Banca Commerciale Italiana—that is to say, the foreign exchange accounting department where this letter was routed to; I went to the claim department; I went to the

169

Vostro Department; I went to the cable department and to the stock department.

Q. And that is all you can say about it? A. Yes, sir.

Mr. Memhard.—I want to offer here, for the convenience of everyone, a translation of the terms used in the statements—perhaps we can agree on it without calling a witness.

It is stipulated that the Italian words appear in the correspondence and statements have the following meanings:

170

Valuta, in conjunction with a date, means the date upon which the funds shall be or were made available.

Mr. Goldmark.—And the date from which interest is paid or charged.

Mr. Memhard.—Is that correct?

The Witness.—Yes.

Mr. Memhard.—Disposizioni annul appearing in Exhibit 19-B means drawings annulled.

I would like to read the whole item in that connection, on the credit side "September 10th, disposizioni annul, 1,526,048.48, September 10th".

171

Dare means debit.

Avere means credit.

Loro means their.

Colla means worth.

Conto means account.

Pagamento means payment.

Causale means items or particulars.

Importo means amount.

172 *Otto H. Schulze for Claimant—Cross.*

The words a riportare means to be carried forward.

Riporto means brought forward.

Bonifico means a payment effected by means of a credit as distnguished from a payment in cash.

The abbreviation disp. list. means drawing list or list of drawings.

Saldo means balance.

Saldo precedenti means previous balance.

Saldo a nuovo means balance to be brought down.

173 Should it become necessary, for an understanding of the record, to translate any other terms, we may reopen for that purpose.

The Master.—Are you finished with the witness?

Mr. Memhard.—I am through.

The Master.—Does the trustee want to cross-examine the witness?

Mr. Goldmark.—Yes, sir.

*Cross-examination by Mr. Goldmark:*

174 Q. Mr. Schulze, are you familiar with the methods employed by the foreign exchange department of the bankrupt? A. I am.

Q. Will you please indicate the sequence of transactions from the time of the receipt of an advice from an inland bank, first, down to the time of the transmission of an advice to the foreign bank? A. Advices come generally with checks attached in payment thereof to Knauth, Nachod & Kuhne in an envelope supplied for that purpose, blue or green, I don't remember which,

printed on Knauth, Nachod & Kuhne. The mail department, knowing the contents or purported contents of those envelopes, immediately distributes those to the advising department; the advising department separated the checks from the advices, checked the amount of the check to see whether it corresponded with the amount that had been figured by the bank on the advices—and at that time they kept the checks separate from the advices; in other words, that was one operation. The checks went to what we may call a deposit teller in the foreign exchange department, who listed on the typewriter all of the checks, giving the bank that had remitted and the bank number that the check was drawn on and the amount thereof. These were totalled up in batches and, when convenient, were then turned over to the assistant in the cashier's department, who then, including checks from all other departments, made up a deposit ticket, and it was then deposited in any one of the deposit banks in New York, of Knauth, Nachod & Kuhne; or, where items were drawn on out of town banks, they may have been sent to the collection department so-called, who would send to the out of town banks, for example Chicago or Milwaukee or any other outside places—

175

176

177

Mr. Trosk.—Do we understand that this is a statement of the general custom or what is supposed to have happened to our particular check?

The Master.—It refers to the general course of business as I understand it.

Mr. Trosk.—Then it has no relation to what happened to our particular check.

178 *Otto H. Schulze for Claimant—Cross.*

The Master.—I don't know, it may have.

Mr. Trosk.—If it is intended to offer this statement with reference to our check, then I object to it as not being identified with our transaction in any way.

The Master.—To what part of the answer does your objection refer?

Mr. Trosk.—Well, I rose to inquire whether the trustee was attempting to prove merely a general custom or what happened in our particular case. I assume that he was trying to prove a general custom
179 and not what happened in our particular case. If I am correct about that, then it seems to me this testimony is not material to our particular controversy and I would suggest that the witness be not allowed to go any further along those lines.

The Master.—Very well, do not go further on this line.

Q. When the advice, Exhibit 6, was made out, what entry was then made upon the books of the bankrupt? A. The total amount represented on the first sheet of Exhibit 6, which we call a recapitulation, was posted to a memorandum ac-
180 count which we call nostro books.

Q. Have you that book here? A. We have the particular sheets here where this amount was credited.

Q. Will you produce that please? A. (Witness produces paper).

Q. Now produce the sheet from the memorandum book which you state includes the entry of the aggregate of the advised drafts covered by Exhibit 6? A. I do.

Q. And that entry is entry No. 5 from the bot-

tom of the page which you hold in your hand? A. Yes, sir.

Q. And this account purports to be what? A. Purports to be the account of Knauth, Nachod & Kuhne with Banca Commerciale Italiana, Genoa.

Q. And it shows advised drafts, does it not? A. It does.

Q. And it also shows deposits which Knauth, Nachod & Kuhne made with the Banca Commerciale Italiana? A. It does.

Q. And the entries were made upon that sheet, were they not, at the time when the advice to the Banca Commerciale Italiana, in the form of Ex- 182
hibit 6, was ready for mailing? A. Yes, sir.

Mr. Trosk.—I assume that the witness knows these things personally, Mr. Goldmark.

Mr. Goldmark.—I think he does, and if he does not, I want him to say so.

The Witness.—Yes, I do.

Q. It is true, then, is it not, Mr. Schulze, that at any moment you are able to ascertain from the account whether the advised drafts at that moment exceeded, in their aggregate the aggregate of credits which the bankrupts had with Banca Commerciale Italiana? A. As per this 183
book, yes, sir.

Mr. Trosk.—I don't quite understand that answer—may we have the last answer stricken out because I think we were at cross-purposes.

The Master.—Read the last question and answer.

(Question and answer read.)

The Master.—I will let it stand.

184 *Otto H. Schulze for Claimant—Cross.*

Q. This account, Mr. Schulze, therefore, is substantially the equivalent of an ordinary check book account, is it not?

Mr. Trosk.—I don't think the witness ought to be led.

The Master.—I sustain the objection.

Mr. Goldmark.—I offer in evidence the page to which the witness just referred.

Mr. Trosk.—There is no objection whatever to that page.

(The page referred to was received in evidence and marked Trustee's Exhibit No.
185 1 of October 24, 1924).

Q. At what time, Mr. Schulze, was the entry of 197,508.60 lire made upon Trustee's Exhibit No. 1? A. It was made as of May 22, 1923—as to the hour or exact date, I cannot testify.

Q. Was it made within twenty-four hours? A. Yes, sir.

Q. It was made practically simultaneously with the preparation of the advice and placed in the mail and addressed to Banca Commerciale Italiana? A. Yes.

Q. And is that equally true of the other entries on that page? A. It is.

186 Q. That is the system by which those entries were made? A. Yes, sir.

Q. Referring to the debit side of the same Exhibit, Trustee's Exhibit No. 1, I find an entry, for example, on May 21st, East River National Bank, 250,000; what does that entry indicate? A. That indicates a purchase from the East River National Bank to be paid to the Banca Commerciale Italiana for our account 250,000 Lire.

Q. What date is May 21st, what date does it

represent? A. May 21st represents the date that the transaction was consummated with the East River National Bank.

Q. Will you state, please, whether on May 22nd, 1923, the aggregate of the credits on that account exceeded or were less than the aggregate of the debits?

The Master.—Read the particular question.

Mr. Trosk.—I object to that, if your Honor please, because the witness has already stated that he cannot tell what the fact was; that the best he can do is to state 188 what these books reflect, but that there were debits and credits in transit and that nobody could tell from these entries what the actual condition of the account was abroad on any given date.

Q. (Read).

The Master.—You mean on this book?

Mr. Goldmark.—Yes.

The Master.—Objection overruled.

Mr. Trosk.—I object to it if it is a question of what the books show.

The Master.—Of course I agree that the 189 books show it, but there is no harm in letting a witness sum up the books for me.

Mr. Trosk.—But it is not a statement of fact, but what the books show?

The Master.—That is all.

Mr. Goldmark.—That is all I am trying to show at this time.

The Witness.—The books show total credits, in Lire, of 47,372,171, and the total debits equal 45,811,298.97 Lire.

190 Q. In order that there may be no misunderstanding when we are speaking now of debits and credits, we are speaking from an accounting standpoint. But putting it in the layman's point of view, it means, does it not, that on that day—

Mr. Trosk.—I object to what it means; he ought to let the witness testify.

Mr. Goldmark.—I am trying to show that the debit means that they owe to us; it is a summary of our drawings; in other words that the amount of drawings exceeded the
191 credit which we had in this book on that date. I don't want any mistake, either here or in any other court, as to what debit and credit mean on that statement.

The Master.—What does it mean on that statement?

The Witness.—Debit and credit on this statement means as follows: The debits represent our purchases of Lire which we supplied to the bank for our drawings; the credits represent our drawings against those purchases.

Q. Now did I understand you to testify that
192 on May 22nd, for example, you don't know exactly what particular debits and credits, which appear in Trustee's Exhibit No. 1, had actually been credited to your account on the books of the Banca Commerciale Italiana? A. No, I do not.

Q. You do not know? A. No, sir.

Q. And despite the fact that you didn't know that on May 22nd, you made no entry on that day, did you, of any liabilities to the claimant in this case?

Mr. Trosk.—I don't understand what you mean by that.

Mr. Goldmark.—I mean on their theory that there was an equitable assignment, if their theory is correct, then until the money was available at the Banca Commerciale Italiana, if our obligation was to assign a balance over there, then we certainly were liable to the Trinidad Bank until that assignment had taken place and the funds were available in Italy.

The Master.—I think that is very speculative. 194

Q. Referring to the trial balance, Mr. Schulze, if on the day that your trial balance was made up you had immediately, prior thereto, sent a check to a creditor in payment of an obligation of Knauth, Nachod & Kuhne, and the trial balance was made up at such a time that the check could not as yet have been collected—for instance, if you sent it to an out of town creditor, would that indebtedness to that creditor be reflected on the balance sheet?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial. 195

The Master.—I overrule the objection.

Mr. Trosk.—Exception.

Q. Do you understand the question? A. Yes, sir. We showed no such liability on our books for a check that had been drawn just prior to the trial balance.

The Master.—In other words, what you did, you made your entries when the check

was drawn as if the payment had been made?

The Witness.—Yes, sir.

Q. Now when you testify that there are no book entries showing any indebtedness or liability, whichever term we use, to the Trinidad Bank, am I correct in understanding that you mean, by that, that there are no entries other than Trustee's Exhibit No. 1, a copy of the advice from Trinidad, the Steamer Block, the acknowledgement from the Banca Commerciale Italiana—what I mean by
197 that is this: Those are underlying records, are they not? A. Yes, sir.

Q. In other words, when you look at this entry to which I have referred, five lines from the bottom of Trustee's Exhibit No. 1, in order to have that entry at all intelligent, you must go back to supporting records? A. Yes, sir.

Q. And those supporting records disclose what the transaction is? A. That is true.

Q. Now what are those records? A. That will be the Steamer Block socalled.

Q. That is, that will show the detail of every advice? A. Yes, sir.

198 Mr. Trosk.—I don't think we ought to characterize what it will show. It is in evidence and your Honor will see that it does not show the details of every advice at all.

The Master.—I will strike out the last answer.

Mr. Memhard.—Why don't you ask him if it does not refer to Exhibit No. 6?

The Master.—He said it referred to the Steamer Block—that is enough.

199

The Witness.—But it isn't the same as the evidence you have here.

Q. What do you mean by the Steamer Block? A. That is only part of it. In other words, that is not our entire Steamer Block record, that is part of it.

Mr. Memhard. The Steamer Block is the book containing the drafts and dates together?

The Witness.—Yes, sir, but it contains more information than is contained in that Exhibit.

200

Q. It shows the dollar rate, does it not? A. It shows dollars—it might show the rates in some cases.

Mr. Memhard.—Well, Exhibit 6 is an exact copy of the Steamer Block, is it not?

The Witness.—It is a copy of a part of it.

Mr. Memhard.—With the exception of the dollar record.

The Witness.—That is right.

Q. And the dollar record which is a copy of Exhibit 6, plus one further, column, that column shows the number of dollars that you got from the Trinidad Bank? A. Yes, sir.

201

Mr. Memhard.—But Exhibit 6 is a complete copy of the Steamer Block of that date, with the exception of the dollar record, is it not?

The Witness.—That is right.

Q. In other words, Exhibit 6 is what was sent abroad? A. Yes, sir.

202 *Otto H. Schulze for Claimant—Cross.*

Q. And that paper was prepared in quadruplicate? A. Yes, sir.

Q. And one of the copies is a little longer than the other copies, is that right? A. Yes, sir.

Q. And that is the copy which becomes part of your office records? A. Yes, sir.

Q. Referring to Exhibit 6-D, is the paper which I now show you the column which is upon the particular copy which is retained as your office file? A. I can prove it if I had a whole set—I just want a summary.

Q. Here is the whole set (handing witness
203 paper). Is the paper which I now show you the column which is part of the office copy of Exhibit 6-D? A. It is.

Mr. Goldmark.—I offer it in evidence.

(The paper referred to was received in evidence and marked Trustee's Exhibit No. 2 of October 24, 1924).

.....

Subscribed and sworn to before me
this day of 1924.

204 .....
Special Master.

Hearing adjourned, by consent, to October 28, 1924, at ten thirty A. M.

*Otto H. Schulze for Claimant—Cross.* 205

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK,

In Bankruptcy.

Before ROBERT P. STEPHENSON, Esq., Special Master.

In the Matter
*of*
KNAUTH, NACHOD & KUHNE,
Bankrupts. 206

32 BROADWAY, NEW YORK CITY,
October 28th, 1924; 10:30 A. M.

HEARING ON RECLAMATION OF FIRST NATIONAL BANK OF TRINIDAD, COLORADO.

Proceeded pursuant to adjournment.

APPEARANCES:

MESSRS. ROSENBERG & BALL, Attorneys for Trustee,
By GODFREY GOLDMARK, Esq., 207
GEORGE G. ERNST, Esq., and
RALPH F. COLIN, Esq., of Counsel.
MESSRS. O'BRIEN, BOARDMAN, PARKER & FOX, Attorneys for Claimant,
By WILLIAM DEFOREST MANICE, Esq., of Counsel,
ALLEN R. MEMHARD, Esq., of Counsel for Claimant.
GEORGE TROSK, Esq., of Counsel for Claimant.

214 *Otto H. Schulze for Claimant—Cross.*

Q. Which meant, did it not, that that was the date on which the money was to be available to you by the Banca Commerciale Italiana? A. Yes, sir.

Q. Now it sometimes happened, did it not, that after a draft had been advised in the method that has been indicated here, you advised the Banca Commerciale, or in other cases other foreign banks, that you cancelled such advice?

Mr. Trosk.—I object to that as incompetent, irrelevant, immaterial, having no relation to the draft in suit, and there is no
215 evidence that the circumstances under which any such notice was given were in any way similar to the circumstances attending this case.

Mr. Goldmark.—Will your Honor hear me on it?

The Master.—Yes.

(Then followed oral argument).

The Master.—I will allow you to show the custom and practice followed between K. N. & K. and the Banca Commerciale Italiana, but not as to all foreign banks.

Mr. Trosk.—We respectfully except, if
216 your Honor please.

Mr. Goldmark.—I will reframe my question, striking out so much as refers at this time to other foreign banks.

The Master.—You had better put a new question.

Q. What was the practice between the bankrupt and the Banca Commerciale Italiana with respect to the cancellation of advised drafts?

Mr. Trosk.—To that question I make the

same objection, also that it is not within the issues.

The Master.—Objection overruled.

Mr. Trosk.—Exception.

A. K. N. & K. would advise the Banca Commerciale Italiana, Genoa, that they desired to have advice in Steamer Block No. so and so cancelled; please do so and advise us and credit our account.

Q. Was it the practice to advise the Banca Commerciale Italiana that such cancellation was at the request of the drawer bank? 218

Mr. Trosk.—I think the witness ought to state what they said and what they did and that Mr. Goldmark ought not to testify for the witness.

Q. Was there a regular printed form used for the cancellation of advised drafts? A. There was.

Q. Have you such form here? A. I believe we have.

Mr. Trosk.—Our objection was to the whole line of testimony, your Honor; I didn't want to interrupt after every question.

The Master.—I think you had better 219
state your objection each time.

Mr. Trosk.—May I have the same objection and exception to each of the questions on this line?

The Master.—I don't think there is any question pending now.

Mr. Trosk.—I mean with respect to the questions already asked since the one I did object to.

220 *Otto H. Schulze for Claimant—Cross.*

The Master.—The last question asked was this: Did you have a form for advised drafts, and he answered yes.

Mr. Trosk.—And I object to that as irrelevant, immaterial and incompetent.

The Master.—Objection overruled.

Mr. Trosk.—Exception.

Q. I show you a paper and ask you if that is the form that was customarily used by the bankrupts in advising the Banca Commerciale Italiana of the request that an advice be cancelled.

221 Mr. Trosk.—I make the same objection, and on the additional ground of form.

The Master.—Overrule the objection.

Mr. Trosk.—Exception.

A. This is one of the forms that we used.

Mr. Goldmark.—I offer it in evidence.

Mr. Trosk.—The same objection, if your Honor pleases.

The Master.—Objection overruled.

Mr. Trosk.—Exception.

(Received in evidence and marked Trustee's Exhibit No. 3, October 28th, 1924).

222 Q. Was it the practice, in transmitting requests to cancel advices in the form of Exhibit 3, to advise the Banca Commerciale Italiana that the cancellation was at the request of the Trinidad Bank or any inland bank?

Mr. Trosk.—I object to that upon the same grounds and upon the ground that the paper in evidence speaks for itself.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. Let me hear the question.

Q. (Read). A. It was not.

Q. Upon the receipt of requests for cancellation in the form of Trustee's Exhibit No. 3, did the Banca Commerciale Italiana in fact cancel the advices requested to be cancelled?

Mr. Trosk.—Same objection.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. It did.

Q. Can you state what entries were thereupon made by them to effectuate that cancellation? 224

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial and, in the very nature of things, this witness cannot know anything about it.

The Master.—Sustained.

Q. Will you state where such cancellations would thereafter appear in statements received by you from the Banca Commerciale Italiana?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial, no evidence that such statements were received.

Mr. Goldmark.—I withdraw the question. 225

Q. You did in fact receive periodic statements from the Banca Commerciale Italiana? A. We did.

Q. In the form of Claimant's Exhibits Nos. 7, 8 and 9? A. Yes, sir.

Q. Was it the practice of the Banca Commerciale Italiana to credit the general account of the bankrupts with the amounts of such cancelled ad-

226 *Otto H. Schulze for Claimant—Cross.*

vices on such statements periodically received by you?

Mr. Trosk.—Same objection, if your Honor please.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. Yes, sir.

Q. And do you know whether there were any credits in these statements?

Mr. Trosk.—I make the same objection.

227 The Master.—Objection overruled.

Mr. Trosk.—Exception.

A. Yes, sir.

Q. I call your attention to Claimant's Exhibit No. 8 and ask you to indicate, if you can, from that exhibit, a credit to the bankrupts for a cancelled draft?

Mr. Trosk.—I object to that on the same grounds.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. On this sheet you show me, the third item
228 on the credit side of this statement shows a cancellation or disposition, 56,925 cancelled, 1,015 lire, value date June 9th.

Mr. Trosk.—Does that refer to a draft?

The Witness.—I don't know whether it refers to a draft or money order.

Mr. Trosk.—That gives you some idea, your Honor, where we are going to be led if we take this kind of testimony.

Q. Was the same practice pursued with respect

to the cancellation of drafts drawn by inland banks?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial and not within the issues.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. It was.

Q. How was the value date for the credit determined?

Mr. Trosk.—Same objection; I think it is entirely immaterial to the issue here. 230

The Master.—Objection overruled.

Mr. Trosk.—Exception.

A. I really don't think I can state how they arrived at the value date.

Q. As of what date? A. Perhaps I didn't hear your question right.

Mr. Trosk.—Are you referring to the item appearing in Exhibit 8 or to the general custom?

Mr. Goldmark.—I am referring to the general custom, as of what date the credit was value dated. 231

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial.

The Master.—Objection overruled.

Mr. Trosk.—Exception.

The Witness.—They would credit our account on the date that they had been able to effect the cancellation. In other words, if I may explain, some of these drafts may have been drawn on their inland correspondents.

232 *Otto H. Schulze for Claimant—Cross.*

Q. You mean their branch banks? A. Their branch banks and, until they had notice that the branch banks had been able to effect cancellation, they would not have been able to make an entry in their accounts, and so notified us.

Mr. Trosk.—I move to strike out the answer on the ground that it appears from the answer that the witness is speculating and has no personal knowledge about it.

The Master.—Motion denied.

Mr. Trosk.—Exception.

233 Q. What practice do you pursue upon receiving a statement in the form of Exhibit 8, indicating a recredit of a cancelled draft?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial and not binding on the claimant.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. That statement would be checked with our memorandum records in the office to determine whether the same entries had been made on their books as had been made on our books.

234 Mr. Memhard.—And you are referring to Trustee's Exhibit No. 1 when you refer to memorandum records?

The Witness.—Yes, sir.

Q. Was this same form as Trustee's Exhibit No. 3 used both in the case of the cancellation of advices of counter-drafts and of drafts drawn by the Trinidad Bank?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial and not

within the issues. There is no proof in this case that there was any cancellation of any drafts by the Trinidad Bank at all. As a matter of fact there wasn't any cancellation and Mr. Goldmark ought not to put that into his question.

Mr. Goldmark.—You make the statement that there was never any cancellation by the Trinidad Bank?

Mr. Trosk.—I say of the draft in suit. As a matter of fact there isn't any proof here that any draft drawn by the Trinidad was cancelled. 236

The Master.—Objection overruled.

Mr. Trosk.—Exception.

A. Yes, sir.

Q. At the time you sent out a request for cancellation in the form of Trustee's Exhibit No. 3, the draft advised was not in the possession of K. N. & K., was it?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial. Some of them may and some of them may not have been.

The Master.—Objection overruled. 237

Mr. Trosk.—Exception.

A. It was not.

Q. K. N. & K. didn't know who had the draft, did they?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial. If your Honor please, this man is an auditor, and I do not think it can be proved by him whether a draft was in the possession of

232 *Otto H. Schulze for Claimant—Cross.*

Q. You mean their branch banks? A. Their branch banks and, until they had notice that the branch banks had been able to effect cancellation, they would not have been able to make an entry in their accounts, and so notified us.

Mr. Trusk.—I move to strike out the answer on the ground that it appears from the answer that the witness is speculating and has no personal knowledge about it.

The Master.—Motion denied.

Mr. Trusk.—Exception.

233 Q. What practice do you pursue upon receiving a statement in the form of Exhibit 8, indicating a recredit of a cancelled draft?

Mr. Trusk.—I object to that as incompetent, irrelevant and immaterial and not binding on the claimant.

The Master.—Overruled.

Mr. Trusk.—Exception.

A. That statement would be checked with our memorandum records in the office to determine whether the same entries had been made on their books as had been made on our books.

234 Mr. Menhard.—And you are referring to Trustee's Exhibit No. 1 when you refer to memorandum records?

The Witness.—Yes, sir.

Q. Was this same form as Trustee's Exhibit No. 2 used both in the case of the cancellation of advices of counter drafts and of drafts drawn by the Trinidad Bank?

Mr. Trusk.—I object to that as incompetent, irrelevant and immaterial and not

within the issues. There is no proof in this case that there was any cancellation of any drafts by the Trinidad Bank at all. As a matter of fact there wasn't any cancellation and Mr. Goldmark ought not to put that into his question.

Mr. Goldmark.—You make the statement that there was never any cancellation by the Trinidad Bank?

Mr. Trosk.—I say of the draft in suit. As a matter of fact there isn't any proof here that any draft drawn by the Trinidad was cancelled. 236

The Master.—Objection overruled.

Mr. Trosk.—Exception.

A. Yes, sir.

Q. At the time you sent out a request for cancellation in the form of Trustee's Exhibit No. 3, the draft advised was not in the possession of K. N. & K., was it?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial. Some of them may and some of them may not have been.

The Master.—Objection overruled. 237

Mr. Trosk.—Exception.

A. It was not.

Q. K. N. & K. didn't know who had the draft, did they?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial. If your Honor please, this man is an auditor, and I do not think it can be proved by him whether a draft was in the possession of

238 *Otto H. Schulze for Claimant—Cross.*

K. N. & K. or whether K. N. & K. knew anything about it. It was, as everybody knows, a large organization with many departments, many heads of departments, many independent departments, and this individual doesn't know everything that K. N. & K. had knowledge of.

The Master.—Overrule the objection.

Mr. Trosk.—Exception.

Q. (Read). A. No, sir.

Q. Now in addition to Trustee's Exhibit No. 3 there was another form which was used when you advised the Banca Commerciale Italiana of the cancellation of drafts, was it not?

239

Mr. Trosk.—Same objection, your Honor.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. Yes.

Q. I show you a paper and ask you whether that was the form which was also customarily used between K. N. & K. and the Banca Commerciale Italiana with respect to the cancellation of drafts?

240

Mr. Trosk.—Same objection, also as to form.

The Master.—Overrule the objection.

Mr. Trosk.—Exception.

A. It was.

Mr. Goldmark.—I offer it in evidence.

Mr. Trosk.—Same objection.

The Master.—Overruled.

Mr. Trosk.—Exception.

(Received in evidence and marked Trustee's Exhibit No. 4, October 28th, 1924.)

Q. When was it customary to use Trustee's Exhibit No. 4?

Mr. Trosk.—Objected to as incompetent, irrelevant and immaterial, and not binding on the Claimant.

The Master.—Objection overruled.

Mr. Trosk.—Exception.

A. We used this form for a two-fold purpose, both for drafts drawn in foreign currency and drafts drawn payable abroad in United States dollars. 242

Q. When did you use it for drafts drawn in foreign currency?

Mr. Trosk.—Same objection, your Honor.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. This form was also used when we had the drafts in our possession, in the possession of K. N. & K.

Q. And Trustee's Exhibit No. 3 when you did not have the drafts in your possession? 243

Mr. Trosk.—Same objection.

The Master.—Overrule the objection.

Mr. Trosk.—Exception.

Q. Why did you have these two different forms, if you know?

Mr. Trosk.—I object to that as immaterial.

The Master.—Sustained.

Q. Do you know the reason why these two forms were used, Trustee's Exhibits Nos. 3 and 4?

244 *Otto H. Schulze for Claimant—Cross.*

Mr. Trosk.—Objected to.
The Master.—Sustained.

Q. What was the purpose of Trustee's Exhibit No. 4 as distinguished from Trustee's Exhibit No. 3?

Mr. Trosk.—Objected to.
The Master.—Sustained.

Q. Were there any other forms used to effect cancellation of advices with the Banca Commerciale Italiana?

245 Mr. Trosk.—Same objection.
The Master.—Overruled.
Mr. Trosk.—Exception.

A. No other forms.

Q. Referring to your books of account, when you drew checks, or when K. N. & K. drew checks upon its ordinary American checking account, for instance, in your general account in the Guaranty Trust Company, when did you make the entries of debit and credit growing out of the drawing of that check?

Mr. Trosk.—Objected to as incompetent, irrelevant and immaterial.
246 The Master.—Sustained.

Q. When you drew checks upon your American bank accounts generally, what was the process with respect to making entries growing out of the drawing of such checks?

Mr. Trosk.—Objected to as incompetent, irrelevant and immaterial.
The Master.—Overrule the objection.
Mr. Trosk.—Exception.

A. Entries were made immediately when the

checks were drawn, crediting the bank drawn upon.

Q. And charging what?

Mr. Trosk.—Same objection.

The Master.—Overrule the objection.

Mr. Trosk.—Exception.

A. It depends on the nature of the transaction. If it were vouchers payable, we would charge vouchers payable.

Mr. Memhard.—What kind of a check is he testifying about? May that not appear?

The Master.—I think the question covered checks on American banks. 248

Q. In making up your balance sheet, and particularly the balance sheet concerning which you testified on your direct examination, was there included, in that statement as your cash item, your checkbook balance or actual balance which you had in fact in the bank on that day?

Mr. Trosk.—I object to that, if your Honor please, on the ground that the witness has already testified that he could not tell, in New York, what balance he had abroad.

Mr. Goldmark.—I am not speaking of abroad. 249

Mr. Trosk.—I didn't notice the question was limited to this country.

Mr. Goldmark.—Will you please read the question.

(Read).

The Master.—Objection overruled.

Mr. Trosk.—Exception.

250 *Otto H. Schulze for Claimant—Cross.*

Q. Do you understand the question? A. Yes, sir. The item on that balance sheet pertaining to cash on hand and in banks represents the balances in New York banks according to our New York collection banks; that is, Chicago and Philadelphia; it represents the balance as appears from our books and not from the banks' books.

The Master.—What books?

The Witness.—The books of K. N. & K.

The Master.—The checkbook?

The Witness.—Yes sir—we had loose checks. We had a control account in the
251 general ledger; we had no actual checkbooks.

Q. As to the accounts in the European banks, what balances did you take to put into this statement concerning which you testified?

The Master.—Balance sheet, you mean?

Mr. Goldmark.—Balance sheet, yes.

A. The balance sheet only reveals the net foreign exchange position.

Mr. Trask.—I object to that as not responsive.

The Master.—I do not think it is re-
252 sponsive, strike it out.

Q. (Read) A. We kept the net balances reflected in each bank, and, from those net totals, we added the debits together and the credits together and took the net figures and showed it in the balance sheet.

Q. In other words, you took your book entries as the basis for that computation? A. Yes, sir.

Q. What do you understand to be the meaning of the term "counter draft?"

253

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial.

The Master.—That has not been brought out on direct.

Mr. Goldmark.—But they put in evidence statements which show transactions between us and the Banca Commerciale Italiana not only with respect to their drafts but in connection with drafts drawn by K., N. & K., their own exhibits.

Mr. Trosk.—There is no reference to a counterdraft anywhere in the case.

Mr. Goldmark.—Exhibit 6-E shows drafts 254
drawn not only by the inland banks, but drafts which they themselves put in.

The Master.—You can ask him what he means by "drafts drawn by ourselves."

Q. Referring to Claimant's Exhibit 6-E, what is meant by the term "ourselves" appearing upon that exhibit?

Mr. Trosk.—I don't think that is subject to explanation by an expert witness; the paper speaks for itself. Under the column "drawn by" it says by "ourselves." We don't need any enlightenment about what that means, and it has nothing to do with 255
the draft in suit.

The Master.—Objection overruled.

Mr. Trosk.—Exception.

The Witness.—Drafts marked "ourselves" in this exhibit mean drafts that are signed by K. N. & K. drawn on their balances abroad

Q. In other words, where K. N. & K. were the drawers of the drafts? A. Yes, sir.

Q. It is a fact, is it not, that those drafts so drawn were advised in the same form as Claimant's Exhibits Nos. 6, 6-A, 6-B and 6-C?

256 *Otto H. Schulze for Claimant—Cross.*

Mr. Trosk.—I object to that on the ground the exhibits speak for themselves.

The Master.—Sustained.

Q. Was that the general practice, to include in these same advices to the Banca Commerciale Italiana, both drafts drawn by inland banks and drafts drawn by K. N. & K.?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial.

The Master.—Overrule the objection.

Mr. Trosk.—Exception.

257

A. It was.

Q. And was the amount of such drafts debited to the general balances of K. N. & K. upon receipt of advices in the same manner as the advised drafts of inland banks? A. Yes, sir.

Q. So that the total of Exhibit 6, for example, is debited to your account by the Banca Commerciale Italiana?

Mr. Trosk.—That is in evidence at least a half dozen times.

Mr. Goldmark.—Exhibit 6 is the summary of K. N. & K. drafts and the inland

258 bank drafts showing an aggregate of 197,000 lire. My question is whether that total is not charged against their account in their statements to the Banca Commerciale Italiana.

Mr. Trosk.—That is already in evidence, that it was.

Mr. Goldmark.—I was not sure whether it was or not; it certainly can't do any harm. Do you concede the fact?

Mr. Trosk.—There is no necessity for a

concession. We have already been over the testimony and it is in evidence.

Q. Did the Banca Commerciale Italiana have a dollar account with K. N. & K. in New York?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. They did.

Q. Did they draw drafts on that account?

Mr. Trosk.—Same objection. 260

The Master.—Overruled.

Mr. Trosk.—Exception.

A. They did.

Q. What was the general practice with K. N. & K. with respect to the charging of advised drafts from the Banca Commerciale Italiana on their dollar account in New York?

Mr. Trosk.—I object to that upon the same grounds.

The Master.—Overrule the objection.

Mr. Trosk.—Exception.

A. When advices were received of drafts drawn 261
on dollar accounts in New York, the bank's account was charged and a draft payable account was credited.

Q. Upon the receipt of a request for the cancellation of drafts drawn on the dollar account, would such request be honored on this side?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial. Your Honor understands, now, that the inquiry

262 *Otto H. Schulze for Claimant—Cross.*

is directed to what K. N. & K. did with respect to the drafts drawn by Banca Commerciale Italiana in an account maintained by Banca Commerciale Italiana with K. N. & K. in New York.

The Master.—Yes. I overrule the objection.

Mr. Trosk.—Exception.

A. May I hear the question?

Q. (Read). A. Might I ask the question where this request came from?

263 Q. From the Banca Commerciale Italiana. A. Upon receipt of such requests from the Banca Commerciale Italiana, drafts would be cancelled and their account would be recredited.

Q. Would the Banca Commerciale Italiana advise you as to who had the draft?

Mr. Trosk.—I object to that upon the same grounds.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. It would not.

Q. Are you able to state what the total credit balance of K. N. & K. was in their general ac-
264 count at the Banca Commerciale Italiana on the evening of May 21st, 1923?

Mr. Trosk.—I object to that question on the ground the witness has already testified he couldn't do it.

The Master.—Objection overruled.

Mr. Trosk.—Exception.

A. I have ascertained what the balance in the general account of K. N. & K. with the Banca

265

Commerciale Italiana was on the date of May 21st from their statement.

Mr. Trosk.—I object to that and move to strike out the answer on the ground that it is obviously hearsay.

The Master.—Objection overruled.

Mr. Trosk.—Exception.

Q. What was such balance?

Mr. Trosk.—Same objection.

The Master.—Sustained as hearsay.

Mr. Goldmark.—I respectfully except.

266

Q. What statement do you refer to?

Mr. Trosk.—I object to that because it refers to a question which has been disallowed.

The Master.—I overrule the objection.

Mr. Trosk.—Exception.

A. I refer to statements that had come to K. N. & K. regularly every week, and it is the statement that has the transactions of May 21st.

Q. What is that statement called, similar in form to what? A. Similar in form to Exhibit No. 7.

267

Q. You mean you can compute, from statements similar to Exhibit 7, the balance in the general account of K. N. & K. at the Banca Commerciale Italiana on the evening of May 21st?

Mr. Trosk.—I renew the objection.

The Master.—I overrule the objection.

Mr. Trosk.—Exception.

A. Yes, sir.

Q. What does such computation show the balance to have been?

268 *Otto H. Schulze for Claimant—Cross.*

Mr. Trosk.—I object to that as incompetent, irrelelant and immaterial and not binding on the claimant.

Mr. Goldmark.—He put those statements in evidence.

The Master.—Well, has he?

Q. What statements, other than those in evidence, do you have to use to find that balance? A. I have to use the statement of May 21st to the 27th, I believe, it is a week's statement—I think the statement prior to Exhibit 7, I am not
269 sure.

Mr. Memhard.—Look at Exhibit 7 and see the dates?

The Witness.—This starts with May 28th and I believe it is the statement just before this one.

Q. Have you that statement here? A. Yes, sir.

Q. Is this the statement which I hold in my hand?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial.

The Master.—Overruled.

Mr. Trosk.—Exception.

270

A. It is.

Mr. Goldmark.—I offer it in evidence.

Mr. Trosk.—I object to this statement upon the same grounds as previously stated. This witness could not state what any balance abroad was based on papers received from the Banca Commerciale Italiana.

Mr. Goldmark.—I confess that that ob-

271 jection comes rather as a surprise in view of the fact that, without any objection, these very statements in precisely the same form for the succeeding weeks were put in evidence.

The Master.—But you did object to them.

Mr. Goldmark.—Not on the ground they were hearsay.

The Master.—What did you do with that statement after you got it?

The Witness.—I computed the balance.

The Master.—I mean at the time you received it, what was done with it?

272 The Witness.—This statement was checked with the accounts we had on our books with the Banca Commerciale Italiana as to whether the entries corresponded.

The Master.—And did they correspond?

Mr. Trosk.—I object to that.

The Witness.—I can't answer that exactly. Generally small differences in the statements would have to be reconciled.

Q. You mean differences of a few Lire one way or the other?

273 Mr. Trosk.—I don't think the witness ought to speculate as to what they probably were.

Mr. Goldmark.—I ask counsel to state specifically what the objection is to this paper.

The Master.—He said it is hearsay and I think he is right unless you show it was accepted by them—then it becomes an account stated.

274 *Otto H. Schulze for Claimant—Cross.*

Q. Can you ascertain what errors, omissions or inaccuracies were discovered in that statement from your books? A. Yes, sir.

Q. Can you do it at this moment? A. No, I am not prepared to it just now.

Mr. Goldmark.—Then I will suspend with the cross-examination on that point for the moment.

I ask that the paper be marked for identification.

(The paper referred to was thereupon
275 marked Trustee's Exhibit No. 5 for identification of October 28, 1924).

Mr. Goldmark.—That is all.

The Master.—Have you finished your cross examination?

Mr. Goldmark.—Yes, sir.

The Master.—There are one or two things about which I am not quite clear and if either side thinks that any questions I put are objectionable, please do not hesitate to make the objection.

By the Master:

Q. Did K. N. & K. keep a double entry set of
276 books? A. Yes, sir.

Q. When the advice was received from the Trinidad Bank, which is in evidence, and the check accompanying it, what debit and credit entries were made on their books? A. There was a debit to the bank in which this check was deposited, the Guaranty Trust or American Exchange National, I am not sure which Bank, and the Nostro account—that is the account they would keep on our books representing our balance abroad, were credited—Nostro meaning our account with them.

Q. Well does Nostro mean your account with the Banca Commerciale Italiana? A. Yes, sir.

Q. The Guaranty Trust Company was debited with the amount of this check? A. Yes, sir.

Q. Was the Banca Commerciale Italiana credited or the Nostro account credited with the same amount? A. It was credited with the same amount in order to determine the profit and loss on the transactions of purchases and sales. The foreign amount is the amount that governs in connection with our balance abroad; the dollars, representing either purchases or sales, are our means of checking as to whether there is any profit and loss on 278
the sale and purchase of Lire with that particular account.

Q. I wish you would explain further what that Nostro account is?

Mr. Goldmark.—Is that Trustee's Exhibit No. 1?

The Witness.—Yes, sir.

Mr. Colin.—The so-called memorandum account.

Q. This account, Trustee's Exhibit No. 1, is headed "Banca Commerciale Italiana, Genoa, Lire." Does this entry mean a credit to that bank? A. It means a credit in foreign amount to 279
that bank.

Q. A credit to that bank of what, dollars, Lire, or what? A. In other words, we credit them with the amount of Lire that we ask them to pay. It is exactly the same kind of an account that we keep with the American Exchange Bank—in other words, there we credit the American Exchange Bank with the checks we have drawn out of the deposits we have made in the bank.

Q. Then I do not see how your books balance

because you have a debit against the Guaranty Trust Company for dollars? A. Yes, sir.

Q. And your only credit is a credit of Lire to this bank? A. There is also a credit of dollars in there, but the dollars represent our conditions as regards the profit and loss on the transaction.

Q. This dollar account here would be reflected again in your profit and loss account? A. If it was a profit and loss, the balance would be reflected. If we take an inventory and put an adjusting entry in this account, we would find out the position in Lire and when we get to an even
281 position, anything over that—it may be a long position or a short position—we would figure the cost of that position and we would put the resulting difference in there, which would be transferred to profit and loss.

Mr. Memhard.—Depending on the day when you took that inventory and the market value of the Lire on that day, isn't that so?

The Witness.—That is so.

*Re-direct examination by Mr. Trosk:*

Q. Mr. Schulze, you have given us some testi-
282 mony here as to what the bank on the other side did when you asked them to cancel, and the kind of notice you sent it when you wanted it to cancel; do you recall that? A. Yes, sir.

Q. Now isn't it a fact that in every case, within the categories you refer to, the notification by K. N. & K. to Banca Commerciale Italiana to cancel was preceded by a notification from the drawer bank to the bankrupts that the draft had been lost or would not be presented to the drawee bank for payment?

283

Mr. Goldmark.—I object to that as irrelevant and immaterial.

The Master.—Overruled.

Mr. Goldmark.—Exception.

Q. Yes or no?

The Master.—Have you the question in mind? Perhaps you would like to hear it again?

A. To the best of my knowledge that is true with reference to inland banks, but I also testified that these forms were also used in cancelling our own advices.

284

Q. I am not now concerned with drafts drawn by K. N. & K., I am concerned only with notifications which you sent relating to drafts which were drawn by the drawer banks under the drawing service. Confining your answer to those banks, your answer is to the best of your knowledge, yes? A. Yes.

Q. And is it not a fact that in the case of the draft that we now have in litigation in this case, no such notification was ever received by K. N. & K. from the drawer bank? A. That is true.

285

Mr. Trosk.—Now on that I ask to strike out all this witness's testimony about what was done in connection with the cancellation of drafts.

Mr. Goldmark.—Will your Honor hear me that?

The Master.—Yes.

(Then followed oral argument).

The Master.—Motion denied.

Mr. Trosk.—Exception.

286 *Otto H. Schulze for Claimant—Re-direct.*

By Mr. Trosk:

Q. I think you stated, Mr. Schulze, on your direct-examination, that on the 19th of May, 1923, the credits in your account with Banca Commerciale Italiana exceeded the debits, you explaining that debit and credit were used in the reverse of their usual significance. Do you recall that? A. Yes, sir.

Q. In making that answer, Mr. Schulze, you were attempting, were you not, merely to tell the Master what the entries on Trustee's Exhibit
287 No. 1 indicated? A. Yes, sir.

Q. You were not attempting to tell the Master that as a matter of fact over in Italy there was less money in that account than there were drafts in the hands of the Italian bank for payment, or outstanding for payment? A. No.

Q. Now in addition to that, isn't it a fact that Trustee's Exhibit No. 1 includes, in the column in which you make your charges, drawings by K. N. & K.? A. On the debit side?

Q. Whatever side you call it—the side on which you charge the foreign account? A. Well, are you pointing to the right or left hand side?

Q. On the right hand side, what do you put
288 there? A. We put all the drawings against that bank.

Q. So my question was correct: On the side on which you list drawings, in addition to drafts drawn by drawer banks under the drawing service, you also included, did you not, drawings by K. N. & K.? A. Yes, sir.

Q. You also included cable transfers by K. N. & K.? A. Yes, sir.

Q. And you also included sales of foreign cur-

rency by K. N. & K., did you not? A. Not in that account.

Q. So with the exception of the foreign currency I was correct when I said that you did include drafts drawn by K. N. & K. on Banca Commerciale Italiana and cable transfers on Banca Commerciale Italiana? A. Cable transfers sold, yes, sir.

Q. Now even on the face of Trustee's Exhibit No. 1, would you be prepared to say that on the 19th day of May, 1923, the credits did not exceed the charges for drafts drawn under the drawing service alone? A. The credits did not exceed the 290 charges.

Q. Would it be easier for you if I call the left side the asset side and the right side the liability side? A. Yes, sir.

Mr. Goldmark.—Why not call them deposits?

Mr. Trosk.—I will call the left hand side deposits and the right hand side drawings, for the purpose of my cross examination.

Mr. Memhard.—The right hand side is what was drawn against the account in Italy and the left hand side is what K., N. & K. put into the account. 291

The Master.—Mr. Schulze, this left hand side is marked debit.

The Witness.—Yes, sir.

The Master.—As a matter of fact, is that meant to be a debit?

The Witness.—We would charge them for moneys that we had placed in their custody.

292 *Otto H. Schulze for Claimant—Re-direct.*

By Mr. Trosk:

Q. You wouldn't be prepared to swear here, would you, that on Trustee's Exhibit No. 1 the credits which appear on the debit side of this account did not exceed all of the charges against the account for drawings under the drawing service on May 19, 1923?

Mr. Goldmark.—I object to that as immaterial.

The Master.—Overruled.

A. Not from that statement, no.

293 Q. As a matter of fact they largely exceeded it, didn't they? Don't you know that? A. No.

Q. Will I simplify it if I leave out the word "largely"—they did exceed it, didn't they? A. I would say most of the time they did.

Q. On the 19th of May, 1923, is the question.

Mr. Goldmark.—What has that to do with it?

Mr. Trosk.—That is the date you asked him about.

Mr. Goldmark.—I asked him about the 22nd.

294 Q. Well, on the 19th and 22nd and at all times in between? A. I could only tell from their statements.

Q. I am asking you to tell me whether, from the appearance of your books, it was not the fact on the 19th and 22nd?

Mr. Goldmark.—I submit that that is incompetent in view of the fact that he objected to the evidence of what their books showed.

295

The Master.—Overruled.
Mr. Goldmark.—Exception.

A. I wonder if I understand your question right.

Q. If you don't perhaps it is my fault.

On the 19th of May, 1923, did the assets in the Banca Commerciale Italiana account exceed the drawings under the drawing service; in other words, was there a balance in favor of the assets as shown on Trustee's Exhibit No. 1? A. Taking it from the date of the entries?

Q. And treating only, as charges against those assets, drafts or money orders drawn under the drawing service? A. I would have to analyze all 296
of these.

Q. You have already told us that it was, generally speaking, always in favor of the assets column if you take only the drawings under the drawing service against those assets? A. I am afraid I couldn't testify to that.

Q. Didn't you tell me that a little while ago? A. Only the drawings.

Q. Did you think I included everything else? A. Yes.

Q. And even when you thought I included everything else you thought it would be in excess on the asset side? A. Yes.

297

Q. Well now I want to know whether that was the fact on the 19th of May, limiting your charges against the account to drawings under the drawing service? A. Well, you see it starts—

Q. Just answer my question? A. I can't tell.

Q. So you are not prepared to tell the Master, are you, that even if you limited the drawings to the drawing service alone, the assets in that account did not exceed the drawings? A. No, sir.

Q. How long would it take you to determine

298 *Otto H. Schulze for Claimant—Re-direct.*

that? A. That starts out with the total figures—I would have to go back until there wasn't any balance.

Q. But there is no reason why you shouldn't start in with the figures at the top, brought forward? A. Why, in those figures you have cable sales and other items that you want me to eliminate.

Q. That is, on the credit side of the sheet, what is carried forward includes figures which take in things other than drawings under the drawing service? A. Yes.

299 Q. Now assume as you received the advice of a draft and sent your advice abroad you immediately charged Trustee's Exhibit No. 1 with the amount of the Steamer Block? A. Credited, yes, sir.

Q. And as soon as you sent any money to the Banca Commerciale Italiana, even though it was sent only by mail, you immediately gave them a charge for that money on Trustee's Exhibit No. 1? A. Yes, sir.

Q. Now drafts that you had so entered in Trustee's Exhibit No. 1 on the day you mailed the Steamer Block were sent by mail abroad, were they not as a rule, to the person who was to pre-
300 sent them? A. Yes, sir.

Q. And they couldn't arrive for a long time, could they? A. That is true.

Q. And then that person might negotiate them, might he not? A. Yes, sir.

Q. And so in that course of dealing it might be a considerable period of time before the draft was really presented to the drawee bank for payment? A. Yes, sir.

Q. And notwithstanding that, your entries here

were made as of the date you mailed the advice? A. Yes, sir.

Q. So it is bound to be the fact, is it not, Mr. Schulze, that this Trustee's Exhibit No. 1 cannot possibly be a correct statement of the condition of K. N. & K.'s balance in the Banca Commerciale Italiana? A. That is right.

Q. There is no doubt about that? A. No doubt, no, sir.

Q. And any figures that you may have given to this Court, based on Trustee's Exhibit No. 1, are not a true picture at all of the condition of the account in Italy, are they? A. Not in Italy, 302
no, sir.

Q. Is it not a fact, Mr. Schulze, that if at the time the bank abroad received an advice from you, it did not have a balance to the account of K. N. & K. against which to charge that draft, they would decline to charge it and credit it to drafts payable? A. That is not true.

Q. So that, as far as you were concerned over here, you felt that they would charge your account and credit drafts payable with the amount of a draft when they received that advice, even though they didn't have sufficient funds of K. N. & K. at that time against which to charge it? A. Yes. 303

Q. Was that the universal practice? A. No.

Q. You mean there were exceptions to that rule? A. Yes, sir.

Q. Were there any well defined exceptions? A. In this particular case?

Q. In this particular case, yes. A. Well, they allowed us an overdraft of some 50,000 lire.

Q. So they would extend you that much credit? A. Yes, sir.

Q. And even though your account was not suf-

ficient to meet a Steamer Block, they would charge your account with the amount of it and credit drafts payable provided, according to your testimony, the excess would not be more than 50,000 lire, is that right? A. Yes, sir, excepting this: I know from the correspondence that that privilege was denied K. N. & K. but I don't know at what period it was denied; you would have to refer to the correspondence.

Q. So there was a period when it was denied? A. Yes, sir.

Q. You don't know when that period was? A.
305 No, sir.

Q. Do you know why? A. No.

Q. Did it come at about the time of the bankruptcy? A. No, sir.

Q. Let me read to you a portion of Claimant's Exhibit No. 11 and see if this will refresh your recollection as to what the custom between you was:

"We would ask you further to note that the following orders are being held in abeyance, not having been debited to the account through lack of funds."

And then follow a number of drafts, the total
306 of which is pretty close to a million and a half lire. A. Did you say drafts in your question?

Q. They say here "That the following orders are being held in abeyance," and then on the next page they include drafts. They declined to charge your account and credit drafts payable with respect to those, didn't they? A. Yes, sir.

Q. And the reason they declined to do it was because they didn't have the funds? A. Yes, sir.

Q. You haven't any doubt that that means that

tney didn't have, or deposit for the account of K. N. & K., sufficient lire?

Mr. Goldmark.—I object to that, his statement as to what the reason was.

The Master.—Overruled.

Q. You haven't any doubt that the meaning of those words as used by the Banca Commerciale Italiana to a layman is that the reason was that they didn't have, in the account of K. N. & K., sufficient to its credit, isn't that right? A. Yes, it says "through lack of funds."

Q. And the lack of funds means in the account 308
of K. N. & K., not because they were financially embarrassed? A. No.

Q. K. &. & K. apparently were, isn't that the point? A. No.

Q. As far as the account was concerned? A. No; it happened to be that the cable transfers didn't go through.

Q. Whatever the reason may have been, the fact is that in the mind of Banca Commerciale Italiana K. N. & K. did not have the money to meet the drafts and orders which K. N. & K. had drawn, is that right? A. Yes, sir.

Q. And that was the fact at that time? A. Yes, 309
sir.

Q. Now they did not decline to charge K. N. & K. with the Steamer Block that contained the draft that is in controversy here, did they? A. No.

Q. They actually did charge K. N. & K. with that? A. Yes, sir.

Q. And they credited drafts payable? A. I don't know.

Q. Don't you know that we have stipulated that in this case? A. I don't know what you stipulated.

310 *Otto H. Schulze for Claimant—Re-direct.*

Q. They did charge the account of K. N. & K.? A. Yes, sir.

Q. And that charge remained in exactly the same state up to the time of the bankruptcy, did it not? A. You mean they did not reverse the charge?

Q. Yes. A. Yes, sir.

Q. You never requested them to cancel that draft, did you?

Mr. Goldmark.—You mean prior to the bankruptcy?

311 Mr. Trosk.—Prior to the bankruptcy—I am talking about K. N. & K.

A. You were talking about the charge for this Steamer Block and I am talking about the drafts

Q. I am talking now about the Trinidad draft, which is Exhibit C in evidence in this case; did you ever ask them to cancel that? A. No.

Q. Did they ever cancel it up to the time of the bankruptcy? A. Not having their statements up to the time of bankruptcy during that period, I couldn't tell.

Q. Is that the best answer you can make to that question? A. Yes, sir.

312 Mr. Goldmark.—It is hearsay otherwise.

Q. Don't you know that in the letter of September 10th, in which they sent you a list of the drafts they were then re-crediting, they included this draft? A. Yes, but I didn't know what they did between the time they charged it and September 10th.

Q. As an accountant don't you know that if they told you on September 10th that they were re-crediting your account with a certain draft,

that indicates they didn't do it on August 1st or September 15th? A. It does not indicate it; they may have made a mistake on their books and not even charged us for it at that time.

Q. But they might have? A. Yes.

Q. You don't know but what they may have made a mistake and that is the reason they didn't do it? A. Well, there are so many things involved, I can't tell what they did until I see their statement.

Q. When you saw their statement, didn't you find out then? A. That was after the receivership. 314

Mr. Goldmark.—I object to that on the ground it is hearsay.

Q. I am talking about your knowledge now. You now know that it was not reversed at the time of the bankruptcy, don't you?

Mr. Goldmark.—Same objection.

The Master.—Overruled.

Mr. Goldmark.—Exception.

A. Yes, sir.

Q. And you know it was not reversed until some time in September following the bankruptcy? A. Yes, sir.

Q. And you know that that was done as a result of a direction given by the trustee or the receiver, don't you? A. Yes, sir. 315

Q. And that prior to that time it had not been done? A. That is right.

Q. Now in September they re-credited your account with a certain amount of money that represented drafts that your receiver or trustee had directed them to cancel; do you recall that? A. Yes, sir.

316 *Otto H. Schulze for Claimant—Re-direct.*

Q. That money that they then re-credited had been out of K. N. & K's. account for a varying period?

Mr. Goldmark.—I object to that as calling for a conclusion.

Mr. Trosk—We have here, in the stipulation, that immediately upon receipt of advice from abroad, the foreign banks would charge the account of K. N. & K. with the amount of the advice and credit it to drafts payable.

The Master.—Now what is your ques-
317 tion?

Mr. Trosk—My question is whether these various drafts, the amounts of which they re-credited in September, being the equivalent of these various drafts, did not represent a fund which had been in the drafts payable account for a varying length of time. In other words, some of these drafts had been drawn earlier than others, but when they re-credited them, they re-credited them all back on a certain day, the 10th of September.

The Master.—Ask him that.

318 Q. They re-credited to your account in September a lump sum, do you recall that? A. Yes, sir.

Q. Which was the aggregate of all the drafts reversed? A. Yes, sir.

Q. The drafts that had been so reversed had been advised abroad at various times, hadn't they? A. Yes.

Q. Some of them going back a considerable period? A. Yes, sir.

Q. As soon as they received the advice, orig

inally, of the drawing of that draft, they ceased paying K. N. & K. interest on that much money, didn't they? A. Yes, sir.

Q. And they continued to pay no interest on that money until September 10th? A. Yes, sir.

Q. So that throughout the entire period that the money was charged against K. N. & K.'s account and credited to drafts payable, no interest was paid on it? A. Yes, sir.

Q. And that was true with regard to the money which was re-credited in September as a result of the receiver's direction? A. Yes, sir.

320

Q. What was the customary way of sending money to Banca Commerciale Italiana by K. N. & K.? A. Mostly by cable.

Q. That method of treatment of the situation by Banca Commerciale Italiana, that is, paying no interest up to the very time that they re-credited those drafts to the account of K. N. & K., you received a written advice of that, didn't you? A. That we had received no interest?

Q. In the advice you received, it was apparent, was it not, that they had given you no interest on any of this money up to the time they re-credited it back? A. Yes, sir.

Q. And you made no complaint about it? A. 321
Of course not.

Q. You did not take the position that they had not given you interest to which you were entitled? A. No—we were lucky they didn't charge us anything.

Q. That was the way you felt about it? A. Yes.

Mr. Trosk.—That is all.

By Mr. Goldmark:

Q. What compensation did the Banca Commer-

322 *Otto H. Schulze for Claimant—Re-cross.*

ciale Italiana get for its part in these transactions?

Mr. Trosk.—I object to that as immaterial.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. The use of the funds until payment of the drafts was effected.

Q. The use of what funds? A. That they had charged the account of K. N. & K.

Q. You mean the fund in the drafts payable ac-
323 count? A. Yes.

Q. And that is the only compensation they got? A. To my knowledge, yes.

Q. Well you didn't pay them anything else, did you? A. No, excepting there were charges for interest when we had overdrafts in the account.

Mr. Memhard.—In the general account?

The Witness.—Yes, in the general account.

Q. But wasn't it your practice, in all your transactions with Banca Commerciale Italiana, that advised drafts should be put in to the drafts pay-
able account?
324

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial.

The Master.—I think that has already been covered.

By Mr. Trosk:

Q. On this question of compensation, Mr. Schulze, you never had any agreement with the Banca Commerciale Italiana to pay them any sum for this service, did you? A. Well—

Q. Just answer my question yes or no, did you ever have a written agreement? A. Well now—

Q. Did you or did you not? A. They would send us letters of conditions and, if we acquiesced, we probably would not acknowledge it by letter.

Q. Was there ever a letter that you received from Banca Commerciale Italiana in which they said, "The condition under which we will handle this account is that we are to have the benefit and use of the money in the drafts payable account"? A. No.

Q. Was there ever any other writing in which that condition was suggested? A. Except by inference. 326

Q. I am not interested in inferences; was there any other writing? A. Not to my knowledge.

Q. Did you ever have any conversation with anyone representing the Banca Commerciale Italiana in which it was agreed that that should be their compensation? A. No.

Q. And all you have attempted to give here is your inference from the fact that the money was in the drafts payable account and that they didn't pay any interest on it, and your inference is that that is what they got by way of compensation? A. I know we got no interest on it. 327

Q. Wasn't that your inference? A. Yes, from banking custom.

Mr. Trosk.—I move to strike out "Banking custom."

The Master.—Motion denied.

Mr. Trosk.—Exception.

Now I offer to prove that the moneys which came into the hands of the bankrupts, relating to the draft in controversy here,

328 ultimately came into the hands of the Trustee and that they are now in his hands.

The Master.—You mean the money paid by the Claimant to the bankrupt?

Mr. Trosk.—Yes, sir.

Mr. Goldmark.—In dollars?

Mr. Trosk.—In dollars. That the sum of $1,191.21 paid by the Claimant in connection with the draft here in controversy was received by the bankrupts and from the bankrupts was received ultimately by the Trustee and that the Trustee now has that money.

329 Mr. Goldmark.—I object to that offer of proof on the ground that the testimony, if offered, would be incompetent, irrelevant and immaterial.

The Master.—On the ground that, even if it were true, it would not sustain the first cause of action?

Mr. Goldmark.—Yes, sir.

The Master.—I will reserve decision on that.

(Then followed oral argument).

Mr. Goldmark.—Without conceding the materiality, competency or relevancy of the

330 fact, and reserving my objection to its competency and my right to strike out the fact, I concede it to be a fact that after the draft in question was presented and payment refused by the Banca Commerciale Italiana, the draft was returned to the purchaser, Bachisio Tabasco, and that thereupon the First National Bank of Trinidad paid to the said Tabasco the sum of $1,128.87 and thereupon the said Tabasco delivered the

said draft to the First National Bank of Trinidad. 331

Is that what you want?

Mr. Trosk.—We accept that concession with thanks.

Mr. Goldmark.—Now I object to the materiality, competency and relevancy of the fact and move to strike it out on the ground that, on no theory is it of any importance to determine that there was any equitable assignment of the fund abroad or that it increases the right of this Claimant to proceed against any such fund if it did exist. 332

The Master.—I will reserve decision on that.

Mr. Goldmark.—Do you rest now?

Mr. Memhard.—Not until we know the ruling on this question.

The Master.—I will deny the motion.

Mr. Goldmark.—Exception.

Mr. Memhard.—May we consider the matter until two o'clock?

The Master.—Yes. 333

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(Whereupon an adjournment was taken to October 28, 1924, at two P. M.)

334 UNITED STATES DISTRICT COURT.

SOUTHERN DISTRICT OF NEW YORK,

In Bankruptcy.

Before ROBERT P. STEPHENSON, ESQ.,
Special Master.

In the Matter

*of*

KNAUTH, NACHOD & KUHNE,
Bankrupts.

335

32 BROADWAY, New York City.

October 28th, 1924, 2.00 P. M.

HEARING ON RECLAMATION OF FIRST NATIONAL BANK OF TRINIDAD, COLORADO.

Proceeded Pursuant to Adjournment.

APPEARANCES:

MESSRS. ROSENBERG & BALL,
Attorneys for the Trustee,
By GODFREY GOLDMARK, ESQ.,
336 GEORGE G. ERNST, ESQ., and
RALPH F. COLIN, ESQ., of Counsel.

MESSRS. O'BRIEN, BOARDMAN, PARKER & FOX,
Attorneys for Claimant,
By WILLIAM DEFOREST MANICE, ESQ., of Counsel.

ALLEN R. MEMHARD, ESQ., of Counsel for Claimant.

GEORGE TROSK, ESQ., of Counsel for Claimant.

Mr. Goldmark.—Do you rest now?

Mr. Trosk.—With regard to the tracing I made a formal offer of proof as to which your Honor reserved decision. Would it be satisfactory to you if we rested our case with the understanding that if your Honor should determine that we have established a case up to the point where tracing becomes material, we will come before your Honor on any day that you fix?

The Master.—Is that satisfactory?

Mr. Goldmark.—Yes.

The Master.—Then I think that will be all right.

Mr. Trosk.—Upon that understanding, then, the 338
claimant rests.

Mr. Goldmark.—The Trustee moves to dismiss the claimant's reclamation claim upon the ground that the claimant has failed to show any right in any moneys which have come into the hands of the Trustee.

The Master.—Do you make that motion as to each cause of action?

Mr. Goldmark.—I make that motion both as to the first cause of action and as to the second cause of action and I move to dismiss the same separately.

The Master.—I will reserve decision on that.

Mr. Goldmark.—I take it that our Honor does 339
not require me to point out specifically my reasons for the motion.

The Master.—No, I don't think so.

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Ralph Dawson, called as a witness on behalf of the Trustee, being duly sworn, testified as follows:

*Direct-examination by Mr. Goldmark:*

Q. Mr. Dawson, what is your present occupa-

tion? A. I am vice-president of the Guaranty Trust Company.

Q. How long have you been such? A. Five years.

Q. How long have you been connected with the Guaranty Trust Company? A. Twenty years.

Q. Please state generally what your duties have been with the Guaranty Trust Company? A. Over a period of twenty years?

Q. Speaking generally, what departments have you been connected with? A. I have been all over the foreign exchange department in every capacity
341 that it affords, from junior clerk, senior clerk, department head, head of every department in the foreign department, junior officer of the bank, auditor of the bank and vice-president of it.

Q. Are you at the moment connected with any particular department? A. Yes, the foreign department.

Q. Were you connected with any banking business prior to your connection with the Guaranty Trust Company? A. Yes, sir, I was with the National Bank of Commerce.

Q. For how long a period of time? A. Oh, I should say about a year and a half, and prior to that with the Western National Bank which
342 merged into the National Bank of Commerce, for another year and a half, and for three years before that with the foreign exchange firm of C. Schumacker & Company.

Q. Speaking now generally, what were your duties at the National Bank of Commerce and the Western National Bank?

Mr. Trosk.—That is pretty remote, your Honor.

Mr. Goldmark.—Do you concede his competency.

Mr. Trosk.—No.

The Master.—Objection overruled.

Mr. Trosk.—Exception.

A. In the National Bank of Commerce and the Western National Bank?

Q. Yes? A. I was a clerk in the various departments, including the foreign department, teller, bookkeeper—I worked generally over the banks.

Q. Are you from time to time in touch with the officers of other banks? A. Yes, sir, very much in touch with them.

344

Q. And in particular with the officers of the foreign departments of other banks? A. Yes, sir.

Q. In the course of your experience in the banking business to which you have just testified, have you become familiar with the business, speaking first broadly, of what is termed international banking? A. Yes, sir, fairly.

Q. The record does not show you smile, Mr. Dawson. Don't be too modest, because the record would show "Fairly" but not your smile.

Mr. Trosk.—I think the witness has answered the question. He said "Yes."

The Master.—I think counsel has a right to inquire what the smile means.

345

Q. When you say "Fairly," what do you mean? A. Well, what I mean is I have become as well acquainted with the international banking business as twenty to twenty-five years of intensive experience in every part of the world and with every part of the world and with all sorts of people and all sorts of banking operations can give me.

Q. Have you become familiar with the practices and usages in connection with both the draw-

ing of drafts by New York banks upon their foreign correspondents? A. Yes, sir.

Q. And also the business of so-called protection of drafts by New York banks, bankers or trust companies on behalf of inland banks? A. Yes, sir.

Q. Have you handled such transactions? A. Yes, sir.

Q. From your observation and knowledge of these types of transactions, have you found that there is a general practice or custom in international banking with respect to the method of
347 charging advised drafts?

Mr. Trosk.—Just yes or no.

A. Yes, there is a custom.

Q. What is that custom?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial.

(Then followed oral argument).

The Master.—I will overrule the objection.

Mr. Trosk.—Exception.

Q. (Read). A. You asked me if there was a
348 custom and I said there was.

Q. What is that custom? A. It is the universal custom, in every part of the world which I have visited or had banking relations with, that the drawee bank, upon receipt of advice from its client that a draft has been drawn on it, immediately charges the current account of that client with the amount of any draft or drafts and sets it aside in a special fund awaiting the presentation of any drafts against that fund.

349

Q. How is that setting aside usually done? A. It is usually done by a charge—

Mr. Trosk.—My objection runs to all of this, or shall I object to each question?

The Master.—I think you had better.

Mr. Trosk.—I object to this on the same grounds and respectfully except.

The Witness.—The practice is to charge the current account of the client with the sum of money and carry it over into another account which is known on the ledgers of most banks as "unpresented drafts drawn," 350
where it is entered in a folio under the name of the bank whose account has been charged. Do you want me to elucidate and give you an example?

The Master.—No, I think that is clear.

Q. Is there also a general practice or custom with respect to the cancellation of advices, after their receipt by the foreign bank and prior to the presentation of the draft for payment?

Mr. Trosk.—Same objection.

The Master.—Overruled.

Mr. Trosk.—Exception.

351

A. May I hear the question again?

Q. (Read). Yes or no, please? A. Yes, there is a custom.

Q. What is that custom?

Mr. Trosk.—Same objection.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. I take it the question means that the drawer

352 bank wants to cancel a draft that has already been drawn and advised.

Q. Precisely? A. A communication of the fact of cancellation by any means he can avail himself of, cable, letter or anything else. Upon receipt by the drawee bank that such draft has been cancelled, a reversal entry is passed, taking the amount of such cancelled draft from the unpresented draft ledger and crediting it back into the current account.

Q. And does that same custom prevail in the case of drafts drawn by inland banks, where the
353 advice is by the New York bank?

Mr. Trosk.—Same objection.
The Master.—Overruled.
Mr. Trosk.—Exception.

A. Yes, because the foreign bank, the drawee bank, does not know the party who is drawing.

Mr. Trosk.—I object to that, if your Honor please; the answer is yes, and I move to strike out the balance.
The Master.—Strike it out.

Q. Is such cancellation ordinarily and custom-
354 arily effected without assiging any reason?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial.
The Master.—Overruled.
Mr. Trosk.—Exception.

A. The drawee bank acts entirely on the orders of its client.

Q. Which is the bank— A. Which is the bank that has the account on its books.

Q. Now, Mr. Dawson, these practices have ob-

tained for a very considerable period of time, have they not? A. A very, very long time.

Q. Is there a generally accepted reason amongst bankers, recognized amongst the people engaged in this business for this practice?

Mr. Trosk.—I object to that as immaterial.

The Master.—Overruled.

Mr. Trosk.—Exception.

Q. Yes or no, please. A. Yes.

Q. Will you please state what those reasons are? 356

Mr. Trosk.—Same objection.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. The original reason for this procedure was the necessity of bankers, in days when they had no Federal Reserve Banks or banks of rediscount, or methods of suddenly raising cash, that when they received intimation from a client that he had drawn on them, immediately, to put themselves in possession of funds to meet their commitments; or a banker would liquidate his investments, enterprises or whatever he was engaged in, to put himself in possession of cash, and the custom 357 arose, since he could not invest his money, but was obliged to hold it, that he didn't pay interest, and he held the money in his box or in his office, useless, awaiting the presentation of the commitment or draft.

Q. How has that practice developed in modern times? A. Well, the practice has hung on in modern times, like a great many other practices, and has been availed of as a means frequently

of compensating a banker for an account that would otherwise be troublesome and a loss. You have many accounts frequently that are active, which, on bare balances in current accounts, are a lot of trouble and a loss in handling that would not be worth while, but there is always a non-interest bearing float that compensates you for the trouble you take.

Q. So that in reality there are two reasons, are there not, generally assigned, namely, to put the drawee bank or banker in a position to meet the
359 drafts which have been advised, and to enable him to use that fund as he may without paying interest thereon to the person who has the account? A. That is right.

Mr. Goldmark.—Your witness.

*Cross-examination by Mr. Trosk:*

Q. When is the last time you were in Italy, Mr. Dawson? A. I have not been in Italy.

Q. When is the last time you were in France? A. 1922.

Q. When is the last time you were in Greece?
360 A. I haven't been in Greece.

Q. Were you ever in Sweden? A. Yes.

Q. Norway? A. Yes.

Q. Denmark? A. Yes.

Q. Russia? A. Yes.

Q. Never been in Italy? A. Never been in Italy.

Mr. Trosk.—That is all.

*Re-direct-examination by Mr. Goldmark:*

Q. Have banks or bankers with which you have

361

been connected done business with the countries which counsel has just alluded to? A. Yes, sir.

Q. Is the practice to which you referred, a practice which is indulged in by the banks in New York when they are drawee banks?

Mr. Trosk.—I object to that as immaterial to the controversy.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. I should say in nine cases out of ten, at least.

Mr. Goldmark.—That is all.

362

Mr. Trosk.—Not universal?

The Witness.—There may be a rare exception, but I am not conversant with it.

The Master.—You said, in explaining the reason for this, that the money was held by the foreign bank in its box, useless. What do you mean by that?

The Witness.—That was in the old days; they used to realize on investments, holding the actual cash, before there were bank notes or bills of exchange or simple instruments of value; they used to collect the actual cash and hold it in the box awaiting presentation, and thereby arose the custom 363 of not paying interest on funds which were awaiting payment out.

The Master—Do they do that now?

The Witness.—No, they don't do that now.

The Master.—What do they do now?

The Witness.—Well, they simply pass a book entry and rely on their general reserve or available cash position.

The Master.—How long have they been

doing the latter, passing a book entry and relying on the general reserve?

The Witness.—Well, I think that point, historically, from where they ceased to realize on investments, is difficult to determine—it may have occurred within the last fifty or sixty years or thirty years.

By Mr. Goldmark:

Q. Your point is, is it not, Mr. Dawson, that in the olden times that you are speaking of, that was the method which drawee banks employed to
365 put themselves in funds to meet these drafts which they knew were coming in for payment? A. Yes, sir.

Q. So that they wouldn't have their own capital tied up in non-liquid investments; is that right? A. Yes, sir—well, they used to realize on their investments.

Q. So as to be in liquid funds to meet the drafts? A. To meet obligations.

By Mr. Trosk:

Q. And the purpose they now serve by doing it by book entry is exactly the same? A. Exactly.

Q. And they tend to accomplish exactly the
366 same result; isn't that right? A. Exactly.

Q. Have you ever seen the books of account of any Italian bank located in Italy? A. No, but I know what they do.

Mr. Trosk.—I move to strike out that he knows what they do.

The Master.—Yes, strike it out.

Q. The answer is no? A. Yes, I have never seen their books of account.

Q. And you have never seen an account book

in Italy, in which there were these transactions that you have recounted for us a little while ago, have you? A. I have seen, from statements from them, how it was performed.

Mr. Trosk.—I move to strike that out.

The Master.—Yes, strike it out.

Q. I ask you if you have ever seen the books of account of an Italian bank located in Italy? A. No.

Q. In which they made the entries that you have attempted to tell us about? A. No.

Q. You made an answer to Mr. Goldmark to 368
the effect that these cancellations were effected upon notification from the drawer, didn't you? A. No, sir, from the client.

Q. Then I may have misunderstood you. A. When the question was asked there was no question of a third party.

Q. You mean the person who drew the draft, when you say client? A. No, sir, I mean the name that is on the books of the drawee bank is the client or the owner of the funds.

By Mr. Goldmark:

Q. You mean the person who has the account in the bank? A. Yes, sir. 369

Q. They cancel the advice at his request whether he is the drawer of the draft or whether he is the person who advised the draft drawn by somebody else? A. Yes, sir; at his order they will cancel the draft.

The Master.—When you said the custom had changed from keeping the money in the box to the present method of making a book entry, does that accomplish the same purpose?

370 The Witness.—Well, we still keep the money in the box, but not specifically. We look over our active liabilities which are imminent, and readjust our cash position in general, but not specifically.

By Mr. Goldmark:

Q. That is, knowing how much the advised drafts are, you know how much money you have to keep as ready cash? A. Yes.

Q. And you determine the amount of drafts which are to come from your general omnibus
371 drafts payable account? A. Yes.

Q. That is, any day, looking at your drafts payable account, you know how many outstanding advised drafts there are, how much that amounts to, and therefore, you know how much available cash you have to have in order to meet that draft? A. Yes.

The Master.—Is there any modification of that?

The Witness.—No, there is no modification, except it is a book position and not a specific position. It is not a particular draft account, but generally the law of averages,
372 based on what we expect to be the likely current demands, which our position would be ready to meet.

The Master.—Under the old system of banks keeping the money in boxes, they didn't have any use of that money, did they?

The Witness.—And they probably earmarked each particular bag for a particular purpose.

The Master.—And under the present system does the bank have the use of that money until the draft is presented for payment?

The Witness.—Yes.

By Mr. Goldmark:

Q. They can lend it on the street? A. Yes.

Q. That is, they could lend a sum equivalent to some one on the street, so that, at any moment, if the number of drafts which had been advised, which came in on a particular day, was more than the average number that came in on another day, 374
you would always know at the beginning of the day how much money you needed from your drafts payable account to meet outstanding drafts? A. Yes.

By Mr. Memhard:

Q. Well that is so because of the present methods and means of having cash instantly? A. Yes, sir.

Q. When you say lend money on the street—A. I mean call money.

Q. That is regarded in banking circles as equivalent to cash in hand? A. Yes—it is one- 375
day cash.

By Mr. Trosk:

Q. You wouldn't lend money that didn't belong to you if you were banker, would you? A. Well, none of our money belongs to us; we are holding deposits.

Mr. Goldmark.—Well, that is a question

376 of law. He is testifying to what they did, no matter whose money it is.

The Master.—You mean that the money the depositors put in is the depositors' money, and not the bank's money?

The Witness.—Well, there is a relationship, of course, between a banker and a depositor; there is a legal relationship of debtor and creditor—I didn't know whether he was talking law or ethics.

Mr. Goldmark.—That is all.

Mr. Trosk.—That is all.

(Witness excused).

377 Mr. Goldmark.—Now I shall attempt to read in evidence the two paragraphs of the stipulation which counsel for the claimant saw fit not to read.

It is stipulated that the following facts are true:

Whenever, prior to the payment of a draft which has been advised abroad in the form of Exhibits 6 to 6-E, the bankrupts notified the Banca Commerciale Italiana to cancel any specific advice or advices, or to stop payment on any draft or drafts covered therein, Banca Commerciale Italiana forthwith recredited the bankrupts' ac-

378 count with the amount of said draft or drafts and at the same time debited the account termed "Drafts Payable" for the same amount. This was done without knowledge on the part of Banca Commerciale Italiana as to whether such draft or drafts were in the possession of the bankrupts, the drawer banks or third persons.

Mr. Trosk.—Don't you propose to read the rest of the same paragraph?

Mr. Goldmark.—No. You may read it. 379
I consider it immaterial.

Mr. Trosk.—I don't like to interrupt you, Mr. Goldmark, but the next sentence to that same paragraph is this:

Subject to proof to the contrary, it is conceded that in every case referred to in this paragraph, the notification by the bankrupts to Banca Commerciale Italiana, was preceded by a notification from the drawer bank to the bankrupts that the draft had been lost or would not be presented to the drawee bank for payment, but in the case at bar no such notification 380
was given by the drawer bank to bankrupts.

Mr. Goldmark.—The point is simply this: I offer the first part, he offers the second part, and I take it you will probably let it in over my objection.

The Master.—Yes.

Mr. Trosk.—With that in, I object to the materiality and relevancy of the first part of the paragraph, it being conceded that in every case referred to in the part read by Mr. Goldmark, the notification by the bankrupts to Banca Commerciale Italiana
was preceded by notification from the 381
drawer bank to the bankrupts that the draft had been lost or would not be presented to the drawee bank for payment, but that in the case at bar, no such notification was given by the drawer bank to bankrupts, showing that we have, in the case at bar, an entirely different situation from that which prevailed in the cases in which such notices were given and accepted.

382 The Master.—I will overrule both objections; they may both go in.

Mr. Goldmark.—Then he is offering that as re-direct?

The Master.—I will allow it in as re-direct.

Mr. Trosk.—Otherwise I would have been obliged to wait until Mr. Goldmark got through.

Mr. Goldmark.—All right; I take an exception to permitting in evidence the stipulated fact beginning with the words, "subject to proof to the contrary."

383 Mr. Trosk.—And I have already objected to the admission of the fact that you read, and I take an exception to its admission.

Mr. Goldmark.—The following facts are stipulated to be true—I am reading from paragraph 11:

The said forms of advice, copies of which are annexed and marked Exhibits 6 to 6-E, included as occasion arose, advices of drafts drawn not only by inland correspondents of the bankrupts, like the claimant, but also drafts drawn directly by the bankrupts. Upon the receipt of advice in the form of Exhibits 6 to 6-E of the drawing of such

384 drafts by the bankrupts, and before such drafts were presented and paid, said Banca Commerciale Italiana thereupon debited the bankrupts' general account referred to in paragraph "9" hereof, with the amount of the draft so drawn by the bankrupts and simultaneously credited the account termed "Drafts Payable" referred to in Paragrap "9" hereof. (Paragraph 9 being one of the paragraphs of the stipulated facts which has already been received in evi-

dence, beginning with the words "When the Banca Commerciale Italiana at Genoa received the papers in the form of Exhibits 6 to 6-E hereof," and so forth).

Mr. Trosk.—We object to that, if your Honor pleases. That relates to what the bank on the other side did in connection with drafts drawn by K. N. & K. Ours, of course, is not such a draft, and we are going outside of the inquiry. This deals particularly with drafts drawn by the bankrupts.

The Master.—I overrule the objection. 386

Mr. Trosk.—Exception.

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Otto H. Schulze resumed the stand, having been previously sworn, further testified as follows:

*Direct examination by Mr. Goldmark:*

Q. Mr. Schulze, since the session this morning have you sought to ascertain whether the statement, Trustee's Exhibit No. 5 for identification, was gone over for the purposes of ascertaining whether it is correct—that is, gone over in the office of the bankrupts? A. I have. 387

Q. What do you find?

Mr. Trosk.—I object to that.

The Master.—Overruled.

Mr. Trosk.—The mere fact that they may have accepted it as true between themselves does not bind us, as I understand it.

The Master.—Objection overruled.

Mr. Trosk.—Exception.

388 *Otto H. Schulze for Trustee—Direct.*

Q. What did you find? A. I found that there were some exceptions, omissions on our books, that were not shown on their books, of which we sent them notice, and they replied to our letter explaining these exceptions.

Mr. Trosk.—I object to that.

The Master.—Yes, sustained.

Q. Have you here the two letters which reconcile those items of which you speak? A. Yes, sir.

Q. Are these the letters that I hold in my hand? A. They are.

389 Mr. Goldmark.—I offer them in evidence.

Mr. Trosk.—On the state of the proof, I object to these statements.

The Master.—I sustain the objection.

Q. Mr. Schulze, the letter which counsel has objected to, bearing date August 24th, has been objected to on the ground that it does not appear to him that it has any relation to Trustee's Exhibit No. 5 for identification specifically, because the letter opens with the statement, "I have examined your statements of the account of K. N. & K. as of June 15, 1923." Can you explain how those two tie together? A. In making this
390 reconciliation of the two accounts, that is, the account we had on our books, and the statement they rendered as to the account on their books, we did not reconcile each weekly statement; they were kept in a folder and, when the clerk had an opportunity, they were reconciled, and the reconciliation covered the period from December 31, 1922, to the last statement that they rendered as of June 15, 1923.

Q. And therefore, in determining the correctness of the specific statements which they say here

391

were the "statements of your account as of June 15, 1923," it became necessary, did it not, as a matter of course, to consider and reconcile prior statements, including Trustee's Exhibit No. 5 for identification? A. Yes, sir.

Q. That, I understand you, was done between you and the Banca Commerciale Italiana by the interchange of these two letters which I hold in my hand? A. Yes, sir.

Q. So that, of necessity, it did require an examination of the statement, Trustee's Exhibit No. 5 for identification? A. Yes, sir.

392

Q. Will you please state when that was received? A. June 11, 1923.

Mr. Goldmark.—Now I offer the letters in evidence.

Mr. Trosk.—I can't see any possible bearing of these letters on the case.

(Then followed oral argument.)

Mr. Trosk.—We will stipulate, if Mr. Schulze will swear that he has been all over this and checked it persnally, and it shows a particular figure, subject to correction we will take Mr. Schulze's figure.

393

Q. You have been over this and checked it personally? A. Yes, I checked the difference and I found what the difference was as reflected in that letter. In other words, I checked from this statement last night, and I checked from this statement and found the difference between the two.

Mr. Goldmark.—Then I offer in evidence Trustee's Exhibit 5 for identification.

Mr. Trosk.—That may be received on the supposition that Mr. Schulze will swear he has checked it and found it to be correct,

394 *Otto H. Schulze for Trustee—Direct.*

or that any inaccuracies will be explained by those two letters. Is that correct, Mr. Schulze?

The Witness.—Yes, sir.

(Trustee's Exhibit No. 5 was thereupon received in evidence October 28, 1924.)

Mr. Goldmark.—Now I offer in evidence the two letters.

The Master.—Does that statement and the corrections shown by those two letters make a correct statement?

The Witness.—Yes, sir.

395 The Master.—Have you made the calculation which you refer to on this corrected statement?

The Witness.—Yes, sir.

(Letter dated Genoa, September 7, 1923, from Banca Commerciale Italiana to Receiver, received in evidence and marked Trustee's Exhibit No. 6, October 28, 1924.)

(Letter dated August 24, 1923, Receiver to Banca Commerciale Italiana, received in evidence and marked Trustee's Exhibit No. 7, October 28, 1924.)

By Mr. Goldmark:

396 Q. Will you now state, Mr. Schulze, from the statements in evidence, what the free balance of the bankrupts was on the books of the Banca Commerciale Italiana on May 21, 1923? A. The value-dated balance on hand on the evening of May 21st, was 65,195.14 lire.

Q. Are you able to state what drafts had been advised prior to May 22nd and were afloat, so-called, on the morning of May 22nd? A. I made those figures up, yes, sir.

Q. Will you state the aggregate of such drafts in lire drawn on the Banca Commerciale Italiana?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial.

The Master.—Overruled.

Mr. Trosk.—Exception.

A. 1,931,302.67 lire.

Q. Will you state the aggregate of the drafts which were advised by the bankrupts to the Banca Commerciale Italiana on May 22nd?

Mr. Trosk.—I object to that as incompetent, irrelevant and immaterial. 398

The Master.—Overruled.

Mr. Trosk.—Exception.

Q. Mailed on May 22nd. A. 241,608.60 lire.

Q. And that included the draft which is the subject of this reclamation proceeding? A. It did.

Q. Can you state whether any further deposits were credited to K. N. & K. on the books of Banca Commerciale Italiana on May 22nd?

Mr. Trosk.—In Italy?

Mr. Goldmark.—Yes.

Mr. Trosk.—I don't think this witness has any knowledge of that.

Mr. Goldmark.—We are predicating it 399 on the very statements which are already in evidence.

Q. (Read.) As shown by their statements.

Mr. Trosk.—I don't think that adds anything to it. Same objection.

The Master.—Sustained.

Q. Do their statements show whether any further deposits, so-called, were valued as available on May 22nd? A. Yes.

400 Q. What does the statement show? A. The statement shows a credit—that is, that we had deposited 18,639.75 lire, value dated May 22nd—entered on the 23rd and value dated on the 22nd. My balance is made up on the basis of value dates.

Q. Claimant's Exhibit No. 1 included a service for so-called dollar drafts, did it not? A. It did.

Q. Which means what? A. That the inland banks, under this service, could also draw drafts payable abroad in United States dollars: (a) which United States dollars would be paid by the foreign bank at the buyer's rate for dollar drafts
401 on New York; (b) in actual United States currency.

Q. By actual United States dollars you mean what?

The Master.—That is very plain.

Q. Were such drafts advised to the Banca Commerciale Italiana? A. Yes, sir.

Q. Was the account of the bankrupts at the Banca Commerciale Italiana charged with such a draft upon the receipt of an advice? A. It was not.

Q. How, if you know, did the Banca Commer-
402 ciale Italiana receive compensation for a transaction such as I have indicated; that is, a transaction where the draft was payable in actual dollars in Italy? A. For actual dollar draft drawings, they made a charge of a commission.

Mr. Goldmark.—That is all.

*Cross-examination by Mr. Trosk:*

Q. Will you tell us what the actual balance was in the Banca Commerciale Italiana, Italy, on June

4, 1923, as shown by their books? A. I would have to check the statement, as I found that was inaccurate, regarding the testimony that I have given. There is a difference of twenty centesimes there.

Q. That won't mean anything on the record. You mean this paper that I have in my hand? A. Yes, sir.

Q. Well, if it is incorrect, it is in some very minor detail? A. Of course, if it is incorrect in a minor detail, I don't know how glaring that may be. There may be quite a decided difference in one day or the next day. 404

Q. If I should tell you that according to this paper that I hold in my hand—

Mr. Goldmark.—I object to referring to a paper which is not in evidence.

The Master.—Overruled.

Q. If I should tell you that on this paper which I hold in my hand it is stated that on the 4th of June, 1923, the balance on the books of the Banca Commerciale Italiana in Italy was 1,045,484.81 lire, you would say that substantially speaking, there was upwards of a million lire there, wouldn't you? That would be fairly safe? A. Yes, taking it over the entire period, the statement is correct. 405

Q. Would it be safe to say there was over a million there on the 4th of June?

Mr. Goldmark.—I object to that as speculative.

The Master.—Overruled.

Mr. Goldmark.—Exception.

Q. I am willing to take an approximation.

It is so large that we can afford to deal in approximations. A. I think that is all right.

Q. It is safe to say that there was million in lire? A. Yes—if that is what the statement shows.

Q. By all means look at it? A. Yes, that is so.

Q. And on the second of June there was about 200,000, wasn't there, approximately? A. Yes.

Q. And on the very day of the second, about 1,300,000? A. That is right.

Q. Now it is a fact, is it not, that the Banca Commerciale Italiana received this particular
407 draft here in suit, the advice of it, I mean, on the 2nd of June? A. Yes.

Q. And they entered it in their books apparently on the 4th? A. Yes, sir.

Q. But as of the 2nd? A. That is right.

Q. And from that date on they stopped paying interest on the amount of money represented by that Steamer Block? A. That is right.

Q. Now K. N. & K. knew all the time, did they not, that a certain interval would elapse between the time they put a draft on board ship or sent a Steamer Block and the time it would be presented? A. Yes, sir.

408 Q. And it was their practice, was it not, to estimate, in their own mind, the time at which these obligations would be presented, with a view to providing the necessary funds at the proper time? A. Yes, sir.

Q. And that they did by cable transfers? A. Yes.

Q. Now, is it not a fact that on the 22nd, they transferred a million lire to Italy? A. Yes, sir.

The Master.—22nd of what?

Mr. Trosk.—22nd of May, 1923.

Q. Which was the day on which this draft began to float? A. That is right,—pardon me.

Q. The morning after? A. It ceased to be afloat then.

Q. No, it was the 22nd of May. A. Oh, I beg your pardon.

Q. It went into the mail, didn't it, on the 21st? A. Yes, sir.

Q. And the very next morning they sent a million lire over there; is that right? A. What date is that?

Q. The 22nd? A. Yes, sir—I was reading from this statement of June 2nd. 410

Q. What were you saying? A. The answer before, when I said, "Yes," I was looking at June 2nd.

Q. Do you want to correct the answer you made? A. Yes.

Q. What would be the correction? A. Their statement does not show the receipt of a million lire.

Q. But I ask you whether or not K. N. & K. did not cable a million lire? A. May 22nd? I don't see that.

Q. How much did they cable on May 22nd? A. 250,000. 411

Q. Didn't they get 250,000 from the Equitable Trust Company? A. They cabled that on the 21st.

Q. Didn't they? A. They cabled that on the 21st.

Q. Did they also, on the 21st, cable 250,000 lire that they got from the Banca Naz del Reduce? A. They cabled that on the 21st.

Q. And didn't they also cable some on the 22nd, 250,000 that they got from the East River Na-

tional Bank? A. They cabled that on the 22nd.

Q. And didn't they cable 250,000 that they got from the Banca di Roma? A. That 250,000 was the only cable that went out on the 22nd, as I heretofore testified.

Q. And on the 23rd they cabled 250,000? A. Yes, sir.

Q. And on the 24th another 250,000? A. That is right.

Q. I mean the bankrupts, when I say "they"? A. Yes, sir.

Q. Am I correct in this, that the 250,000 which
413 was sent on the 21st, purchased from the East River National Bank, was sent as of value date May 23rd? A. Yes, sir.

Q. 250,000 sent from the Banca Naz del Reduce of the value dated May 22nd? A. Yes, sir.

Q. 250,000 on the 21st that they got from the Equitable Trust Company, value dated the 23rd? A. Yes, sir.

Q. 250,000 from the Banca di Roma, sent on the 22nd, value dated the 24th? A. Yes, sir.

Q. And 250,000 sent on the 23rd from the Credito Italiana Genoa was value dated the 24th? A. That is right.

414 Q. Isn't it also true that as far back as May 11th, they had been sending large sums to the Banca Commerciale Italiana as of value dates around the 23rd or 25th? A. There were no cable transactions valued as late as the 25th.

Q. So they did send money,—when I say "they" I mean the bankrupts. I am not interested in whether they sent cables or anything else, but they did send large sums as early as the 11th, which were to become due around the 23rd, 24th and 25th of the month, didn't they? A. Yes, sir.

Mr. Trosk.—That is all. 415

Mr. Goldmark.—That is all of Mr. Schulze.

The Trustee rests.

I renew my motion to dismiss the claim on the ground that the claimant has shown no right, in its own right, in any funds which are in the hands of the trustee, and has shown no right, in itself, as an assignee or as being subrogated to the rights of the payee, or of any other person, in any fund in the hands of the Trustee. I would particularly call your attention to the fact that if their claim should be construed to proceed in the right of the payee and that they 416 are subrogated to the rights of the payee, the rights of the payee are of necessity determined by the laws of Italy, and there is no proof here offered by the claimant as to what the law of Italy is, and your Honor is not in a position to indulge in any presumptions as to what the law of Italy may be.

So that, upon both grounds and as to both causes of action, I move to dismiss on the ground that the claimant has not shown that it is entitled to any of the funds which have come into the hands of 417 the Trustee.

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Hearing closed.

Decision reserved.

Briefs to be submitted.

418

**Claimant's Exhibit 1.**

(Note. This Exhibit was a book called "List of Foreign Correspondents," the first twelve pages of which are here reprinted in full).

## FOREIGN EXCHANGE

To Our Correspondents:

The constantly increasing demand for Foreign Exchange, on the part of the public, has led progressive banks throughout the country to add the necessary equipment to their general banking ar-
419 rangements to enable them to meet the requirements of their customers, in the matter of drafts and money order payments in foreign currencies. Inasmuch as the maintenance of a Foreign Department, involving the carrying of balances abroad, etc., is undesirable, from the standpoint of a majority of inland banks, we have aimed for many years to supply this want by extending to our correspondents the privilege of using our world-wide facilities for carrying on a foreign exchange business.

Under our arrangements banks and bankers who are provided with our papers issue their own
420 drafts as Principals on the places mentioned in our list of correspondents. Upon receipt of proper advices, and New York funds to cover such drafts at the rates quoted by us for the day on which the drafts are sold, our advices are at once forwarded and funds provided with the respective drawee banks for the payment thereof, by transfers of credit from our balance or otherwise.

Our list of correspondents has been carefully arranged to include a leading bank in nearly every

city and town of importance. For smaller towns or villages, which are not included in our list, we recommend the use of K. N. & K.
Moneys Orders, the advantages of which are fully described herein.

The efficiency of the service which we are able to render depends to a great extent upon the measure of co-operation which we receive from our domestic correspondents, and we urge upon all our friends the advisability of studying the following pages carefully in order to be fully informed as to the terms and conditions under which the above described service is rendered. 422

KNAUTH, NACHOD & KUHNE.

TERMS AND CONDITIONS

GOVERNING THE USE OF K. N. & K. DRAWING SERVICE

(1) Upon receipt of advice of draft, accompanied by adequate funds payable at par in New York, we shall promptly forward our advice of the same and provide the drawee with funds sufficient for the payment of the draft abroad, by a transfer of credit from our balance, or otherwise, 423 PROVIDED THE DRAFT IS DRAWN ON A BANK NAMED IN OUR LATEST LIST OF CORRESPONDENTS.

Under this arrangement, our correspondents in this country act as PRINCIPALS, and issue drafts in their own names, our name not appearing thereon. In other words, we are employed merely as the agents of the drawers for the purpose of advising the issue of their drafts and providing the drawee banks with sufficient funds to cover their payment.

424 *Claimant's Exhibit 1.*

(2) DRAFTS MUST BE SIGNED IN THE NAME OF THE ISSUING BANK OR BANKING FIRM, and, when signed by an officer of an incorporated bank, his official title must be stated.

(3) DRAFTS MUST BE ISSUED IN THE CURRENCY OF THE COUNTRY ON WHICH THEY ARE DRAWN, AS INDICATED IN OUR LIST OF CORRESPONDENTS, WITH THE EXCEPTION OF DOLLAR DRAFTS AS DESCRIBED ON PAGE 5, PARAGRAPH 15. For example, drafts on England must be drawn in Sterling Pounds, Shillings and Pence; drafts on France in Francs and Centimes;
425 drafts on Germany in Marks and Pfennigs; etc.

(4) DRAFTS DRAWN ON FRANCE must have the date spelled out in full, as for example

January twentyseventh 1922

If figures, or other contractions, are used in the date, the draft will be subject to a special French tax for bills of exchange.

(5) DRAFT FORMS are supplied by us, and should be used exclusively, as they are well known throughout Europe and therefore serve to identify the drawers to our friends abroad as being our correspondents, which is of importance to the
426 holders of the drafts.

(6) SPOILED OR VOIDED FORMS should be sent to us marked "VOID" in order that a complete record may be kept in our files.

(7) LOST DRAFTS may be replaced by duplicates; or the face amount may be refunded (after cancellation of advice has been effected abroad and re-transfer of credit has been received by us), at the prevailing purchasing rate when such re-transfer of credit is received, less actual expense in-

curred. In such cases we require a bond of indemnity or written guarantee to hold us harmless should the draft be cashed subsequently by an innocent holder.

(8) DUPLICATES should be issued on special forms, which will be supplied by us upon application, and must correspond in every particular with the original; including Number, Date, Payee and Amount. All duplicate drafts must be plainly marked "DUPLICATE, TO BE PAID ONLY IF ORIGINAL UNPAID," and must be advised to us as soon as issued, in order that we may authorize payment abroad. To COVER THE EXPENSE OF THIS SERVICE, A CHARGE OF 25 CENTS IS MADE. 428

(9) UNPAID DRAFTS sent to us for redemption are purchased by us, WHEN PROPERLY ENDORSED AND THE ENDORSEMENT GUARANTEED BY THE DRAWER, at the buying rate prevailing at the time they reach us. In this connection it should be borne in mind that the value of a foreign draft must be considered in terms of the currency which it represents and not the original dollar amount paid for same. Consequently should such draft remain unpaid, and be presented to us at a later date for redemption in dollars, the foreign amount only must be taken into consideration, and THE AMOUNT OF DOLLARS TO BE RETURNED BY US WILL DEPEND ENTIRELY ON THE VALUE OF THE RESPECTIVE FOREIGN CURRENCY AT THE TIME SUCH REDEMPTION IS MADE. 429

This point is of the utmost importance and should be fully explained to all purchasers of foreign drafts.

(10) ADVICES OF DRAFTS MUST BE MAILED TO US ON THE DAY OF ISSUE. The letter containing the

advices should not be registered but should be sent to us by ordinary mail, addressed "KNAUTH, NACHOD & KUHNE, BANK DELIVERY, NEW YORK, N. Y." Mail so addressed is received by us more promptly than if it bears our street address.

(11) IDENTIFICATION of a holder of a draft may be best accomplished by sending to us, with the drawer's advice, three specimens of the payee's signature to be forwarded by us to the drawee bank. This precaution is advisable for the reason that in most European countries possession is legally sufficient proof of title to warrant pay-
431 ment, and, therefore, European banks do not require any other identification of an apparently rightful holder, and are not legally liable in case it afterwards transpires that either the possession or an endorsement was wrongful. For this reason all drafts should be mailed abroad under registered cover, in order to lessen the possibility of loss. THE OWNER WILL HAVE NO RECOURSE, IN THE EVENT OF A DRAFT BEING PAID TO THE WRONG PERSON THROUGH NO FAULT OF THE PAYING BANK.

Drafts drawn on places in Great Britain, Ireland and France may be protected by "crossing" same. This is done by drawing two parallel lines,
432 about half an inch apart, across the face of the draft from top to bottom and writing "& Co." between these lines. This makes it necessary for the payee to present the draft through a bank, which bank then becomes responsible for the endorsement.

A similar measure of protection may be accorded to drafts drawn on places in Germany by writing on the face of the drafts the words "Nur zur Verrechnung."

REGISTERED MAIL SHOULD ALWAYS BE EMPLOYED IN THE SENDING OF DRAFTS ABROAD.

433

The foregoing facts should be brought to the attention of all purchasers of drafts.

(12) PAYMENT OF DRAFTS ABROAD is not usually reported to us; and we can only ascertain whether or not drafts have been presented for payment by making special inquiry of the drawee bank.

Requests for information regarding drafts should contain a reference to our REPORT NUMBER, which will be found on our card acknowledging receipt of the original advice.

(13) RATES, at which we are prepared to sell, or provide for the payment of drafts, are fur- 434
nished to our correspondents by means of our rate cards or by telegraphic quotations. The rates quoted on our rate cards are to be used only on the dates printed thereon, and only for a total amount, in any one currency, of not more than the equivalent of the dollar limit appearing at the top of the card. For additional sales, making a total beyond said limit, special rates must be obtained by telegraph. Cost of telegrams will be borne by us, if our quotation be accepted. Since our rates are the net figures at which drawers must remit to us, it follows that their selling rates should include their profits.

When telegraphing for special rates, the ap- 435
proximate amount required must be stated, together with the name of the city on which the drafts are to be drawn.

If a remittance be made at a wrong rate, we may return same, or hold it and advise the remitter of the deficit or excess, or, if the remittance be insufficient, we may advise the draft abroad and require payment to us by the remitter of the deficit at the correct rate. If the remittance be

436 *Claimant's Exhibit 1.*

more than sufficient, we may advise the draft abroad and return the excess to the remitter.

(14) DRAFTS ON PLACES NOT ON OUR LIST should be bought from us, and such orders must be accompanied by New York funds to cover. If desired, we will mail drafts direct to the payees, postage and registry fees to be paid by the purchaser, but, in so doing, we will act as forwarders only, and without responsibility for delays which are beyond our control, or for any loss which may result therefrom.

437 (15) DRAFTS IN U. S. DOLLARS PAYABLE AT DRAWEE'S BUYING RATE FOR BANKER'S CHECKS ON NEW YORK.

(*See page 77 for special list of correspondents on which such drafts may be drawn.*)

All drafts drawn as above must bear the following notation:

"PAYABLE AT DRAWEE'S BUYING RATE FOR BANKERS' CHECKS ON NEW YORK, OR BY KNAUTH, NACHOD & KUHNE, NEW YORK, AT PAR."

Remittance to be made to us by funds on New York, plus commission as follows:—

438 For amounts under $1,000. ½% Commission, minimum 50¢ per item.

For amounts of $1,000. and under $5,000. ¼% Commission.

For amounts of $5,000. and under $10,000. ⅛% Commission.

For amounts of $10,000. and up 1/16% Commission.

We have made arrangements, whereby all dollar drafts are payable at par in New York, for the following reasons:

FIRST, because dollar exchange on New York is likely to bring a better price abroad.

SECOND, because it thus becomes possible for the purchaser of such a draft to redeem it in New York for the full dollar amount if for any reason he should not send the draft abroad.

We believe that these features will be greatly appreciated and would therefore suggest that special care be taken to write or stamp the complete phrase as above on each dollar draft.

TERMS AND CONDITIONS GOVERNING THE USE OF K. N. & K. MONEY ORDER SERVICE. 440

Our money order service is designed to furnish to our correspondents in this country safe and inexpensive facilities for transferring funds to Europe for their customers.

The system of making remittances by money order is, in many instances, preferable to the use of drafts, particularly in the countries of Central Europe, or wherever the payees reside in villages remote from banking facilities.

In accepting payments for execution by means of money orders, our correspondents act as PRINCIPALS, and, in forwarding their instructions for the execution of such orders, we act as their 441 agents and without responsibility for loss or delay due to causes beyond our control.

(16) ADVANTAGES OF K. N. & K. MONEY ORDERS.

K. N. & K. money orders are especially desirable for the following reasons:

(*a*) Many persons in the more remote parts of Europe frequently experience difficulty in cashing drafts, owing to their unfamiliarity with bank-

442 *Claimant's Exhibit 1.*

ing rules and customs. K. N. & K. MONEY ORDERS overcome this difficulty, as the money is transmitted for delivery direct to the recipient through the nearest Post Office, or other medium best adapted to existing conditions.

(*b*) In many European countries the laws with regard to the identification of the holders of drafts differ from the laws in the United States. In this country the holder of a check must be identified to the full satisfaction of the paying bank, and such bank is legally liable if payment is made
443 on a forged endorsement. In most foreign countries, however, *the person having the draft in his possession is presumed to be the rightful owner*, and there is no liability on the part of the drawer or the drawee if a draft is paid in good faith to an apparent holder on the presentation thereof.

(*c*) Similarity of name, inaccurate address, theft, or other contingency is often responsible for the delivery of letters containing drafts to wrong persons who may cash them. These risks of loss are materially lessened by the use of K. N. & K. MONEY ORDERS, as under this system our correspondents do not issue a negotiable instru-
444 ment, such as a draft or check, but merely forward instructions abroad, through us, to have the payment made through the mediation of the Post Office, or through a bank or other agency, located near the place of destination.

There are a few countries in Europe, however, where the postal service is not organized to handle remittances of this kind, notably, *Greece, Turkey and Spain*. For this reason the issuance of money orders to these countries is not desirable, and remittances should be made by drafts.

*Claimant's Exhibit 1.*

445

In *Great Britain and Ireland* banking facilities are very highly developed, even in the smaller towns and villages, and remittances to these countries also should always be made by drafts on places named in our list.

(17) APPLICATIONS FOR K. N. & K. MONEY ORDERS should be written by the purchaser and must include the full name and complete address of the recipient.

Special care should be taken to see that the names of the village, post office, county, province, or state are inserted.

446

When such information is available, the name of the street and the house number of the recipient should also be given.

It is advisable to ascertain from the purchaser whether or not any other person bearing the same, or a similar name resides at the place of destination. If so, a more detailed description of the payee should be furnished, giving the name of the recipient's father or, should the payee be a married woman, her maiden name. These details will help materially in locating the proper benecifiary.

If the purchaser of a K. N. & K. MONEY ORDER is not able to make the application out in English, he may do so in his native language and script. 447

In advising us of money orders, it is important to state the correct currency of the countries where the orders are payable, such as Norwegian Kronor, Swedish Kronor, Czecho-Slovac Kronen, Austrian Kronen, Hungarian Kronen, etc. When a doubt exists as to the Country to which a certain place belongs, it is advisable to ask the re-

448 *Claimant's Exhibit 1.*

mitter for an envelope in which he has recently received a letter from the payee. The postage stamp will serve as a guide in determining the country in which payment is to be made.

In order to detect possible errors or omissions, all applications are gone over very carefully by our staff of experienced clerks, who are familiar with the languages of most foreign countries. Notwithstanding this, however, it is of the greatest importance that the necessity for accuracy and explicitness be impressed upon the remitter, with a view to minimizing the possibility of mis-
449 takes.

(18) MONEY ORDER FORMS are supplied by us. These forms are to be used for money orders only and NOT for cable transfers or the issuance of drafts. Special money order advice lists printed in Italian will be furnished by us if required.

In addition to the money order forms we furnish a NOTIFICATION SLIP, printed in many languages, notifying the payee that a remittance has been made and informing him what steps to take in the event of the payment being delayed.

(19) EXECUTION OF MONEY ORDERS depends
450 largely on the accuracy of the information furnished by the remitter.

Orders received from correspondents in this country are promptly advised to our correspondents abroad, for transmission to the payees, in the manner best adapted to conditions existing in the country of destination. Transmission may be effected by bank payment, by post office money order, by cash contained in registered and insured letters, or through some other reputable agency, at the option of our correspondents. The orders

451

will be executed in currency which is lawful money in the place of destination, at the time of execution. Proper notice will be given to the remitter should we receive advice from abroad that a payment cannot be made on account of inaccurate address, or for any other reason.

All payments are effected subject to the laws and customs of the country of destination, and we are not responsible for loss arising from causes beyond our control.

As a rule payments are made against receipts which are forwarded by us to the remitting correspondents as soon as they are received in our 452
office. In some instances, however, such receipts are unobtainable, and, when this is the case, a statement of delivery by the foreign post office or other reputable agency will be furnished if possible. Such receipts or statements must be accepted by our correspondents and remitters as proof of payment.

(20) CLAIMS FOR NON-PAYMENT OF ORDERS, cannot be entertained until a reasonable length of time has elapsed to allow for the receipt of returns from our correspondents abroad. In the event of a change in the address of the recipient named in a money order, we should be informed 453
thereof without delay, and an additional sum of 25¢ should be sent to us to cover the expense of readvising the remittance. We assume no responsibility for delays, or other possible causes of loss, which are beyond our control.

Requests for information regarding K. N. & K. Money Orders should contain a reference to our Report Number, which will be found on our card acknowledging receipt of the original advice.

454 *Claimant's Exhibit 1.*

(21) REFUNDS AND CANCELLATIONS. Inasmuch as we establish credits for the payment of money orders, when advising them abroad, it follows that, when such orders are cancelled, *we can make refund only of the foreign amount which is returned to us, or the equivalent in dollars at the purchasing rate of exchange prevailing when the funds are again at our disposal.* In such cases should the value of the exchange have declined, the remitter must bear the loss, while in the event of an advance in the rate, he will make a profit.

We do not assume any responsibility for fluc-
455 tuations in exchange rates.

(22) RATES, at which we are prepared to sell exchange for money order remittances, are furnished by us in the same manner as we furnish rates for drafts.

OUR CARD QUOTATIONS MUST NOT BE USED FOR AMOUNTS IN EXCESS OF THE SPECIFIED LIMIT FOR A GIVEN DAY AND COUNTRY. Special quotations for amounts exceeding such limit should be obtained from us by telegraph.

The rates which we quote are the net figures at which remittances must be made to us; and, in order to make a profit, selling banks should
456 charge their customers a somewhat higher rate.

If a remittance be made at a wrong rate, we may return same or hold it and advise the remitter of the deficit or excess, or if the remittance be insufficient, we may forward the order abroad, and require payment to us by the remitter of the deficit, at the correct rate. If the remittance be more than sufficient, we may forward the order abroad and return the excess to the remitter.

(23) ADVICES MUST BE FORWARDED TO US IN DUPLI-

457

CATE ON THE DAY OF ISSUE. If an advice be delayed by the selling correspondent, such correspondent will be liable, in the event of an advance in the rate of exchange, for such difference as may have occurred in the interim.

(24) DEPOSITS WITH FOREIGN BANKS should always be made by money order, and not by draft.

When the amount of a money order is to be deposited with a bank abroad, it is necessary to state, in the advice, whether the amount is to be deposited in a checking account or in a savings account; and in the latter case for how long a term.

458

Banks abroad insist upon having the full name and address of a depositor, also his signature, in triplicate, for the purpose of identification. This information should be included in the advice of the money order and the specimen signatures should be attached thereto.

For a deposit with the Postal Savings Bank at Vienna or Budapest, it is also advisable to state when, and where the depositor was born, and to furnish a pass-word which can be transmitted to the bank in question, as a means of identification. Deposits with the Italian Postal Savings Bank (Casse Postale di Risparmio) can be made only with the head office at Rome, and, in such cases, it is necessary to state the name of the depositor's father and whether or not he be alive. This is indicated by writing the word "di" before the name in case the father be living, or "fu" in case the father be dead.

459

DOLLAR REMITTANCES

(25) Purchasers of money orders may desire sometimes to have their funds transmitted abroad

460 *Claimant's Exhibit 1.*

in U. S. Dollars. It should be understood, however, that, foreign banks will not always pay out actual U. S. currency, but will convert the dollar amount into the currency of the country in which the payment is to be made at the then prevailing rate of exchange.

Under government regulations in some European countries payments for goods exported, must be made in dollars. In the case of dollar remittances to private individuals, however, it should be pointed out to the purchaser that, should the rate of exchange advance before payment can
461 be made, it will naturally be to the recipient's disadvantage.

MONEY ORDERS PAYABLE AT THE DRAWER'S BUYING RATE FOR BANKERS' CHECKS ON NEW YORK, may be issued to the following countries:

| | | |
|---|---|---|
| Austria | Germany | Norway |
| Belgium | Greece | Palestine |
| Bulgaria | Hungary | Roumania |
| Czecho-Slovakia | Italy | Serbia |
| Denmark | Jugo-Slavia | Sweden |
| Esthonia | Latvia | Switzerland |
| Finland | Lithuania | Syria |
| France | Luxembourg | Turkey in Europe |

462

For all money orders issued in U. S. DOLLARS PAYABLE AT THE DRAWER'S BUYING RATE FOR BANKERS' CHECKS ON NEW YORK, we must be covered by funds payable in New York at par, including ½% Commission, minimum 50 cents per item, as well as the usual postage fee indicated on our rate cards for the respective countries.

*Claimant's Exhibit 1.* 463

CABLE TRANSFERS

Orders for the payment of money may be forwarded also by means of Cable Transfers.

Such transfers are subject to somewhat higher rates than drafts and money orders, owing to the fact that funds transmitted by cable are available immediately upon receipt of our cable order, and there is no loss of time during transit from New York to the place of payment.

To enable our correspondents to arrive at the proper rates and cable fees, a table has been prepared to indicate how many points are to be added 464
to our quoted MONEY ORDER RATES, and also what amount is to be added for cable charges. This table will be found on page 82. The charges indicated in the table are computed on the basis of a six word address. If the address exceeds this number of words, the additional cost can be readily determined as the cable fee per word to each country is also given. The cable companies count each word of more than ten letters as two words and charge accordingly. This must always be taken into consideration and the number of letters in each word should be carefully counted. Note especially that the MONEY ORDER, not the check 465
rate, is to be used as a basis for determining cable rates.

Instructions concerning the payment of money by cable should always be furnished to us over an official or authorized signature, and "open" telegraphic instructions should always be avoided. Orders may be sent us by telegraph in American Bankers' Association code by members of the Association, or a series of test words may be arranged to protect "open" messages.

466 *Claimant's Exhibit 1.*

Orders for cable remittances will be executed only against cash or a certified check on New York, or against a credit balance on our books. In the case of telegraphic orders remittance to cover should be made by wire, unless a credit balance exists against which the amount can be charged.

As a rule, senders' names need not be mentioned in cable transfers, but in the case of a transfer to a commercial house or bank, it is essential to state in the message for whose account the remittance is made, otherwise such commercial house
467 or bank will be unable to properly credit the funds.

In case of immigrants en route, senders names should be stated, as this is often the only means by which proper identification of the payee can be made.

Cable transfers should be issued in round amounts, if possible. In case it is necessary to forward odd amounts, it must be remembered that an extra charge is made by the cable companies for more than five figures in the amount, and the cost of the extra words must be added to the cable charges.

The execution of cable payments is ordinarily reported to us by mail. If a report by cable is de-
468 sired, additional words in the message will be necessary and the cost of such additional words, as well as the cost of the reply, must be included in the remittance to us.

It is very important to give complete names and addresses of beneficiaries, in order to insure the delivery of the funds to the proper parties. Registered cable addresses can be used under special arrangement only; otherwise, being unknown to our correspondents abroad, they will merely delay the payment.

For frequent cable transfers of large amounts to the same payee, we are able to make arrangements which result in lessened costs for cable charges. Full particulars will be furnished on request.

FOREIGN CURRENCY DEPOSITS.

For the convenience of our customers we have made arrangements whereby we are able to accept deposits in the currencies of any of the European countries quoted on our rate cards, with the exception of Poland, provided the amount to be de- 470
posited is not less than the equivalent of $500.

Interest on the foreign amount will be credited quarterly as long as such foreign amount equals or exceeds the equivalent of $500. at current exchange rates.

We shall be happy to furnish details, and rate of interest, upon request.

FOREIGN COLLECTIONS.

All bills of exchange, sight drafts with documents attached, etc., sent to us for collection, must be endorsed to us in writing, as European banks
will not recognize rubber stamp endorsements. 471

We cannot collect bonds or coupons of lottery issues, their transmissions through the U. S. Mail being illegal.

Our charges for all collections (except by Power of Attorney) are one quarter per cent. for amounts less than $1,000.00, and one eighth per cent. for items of $1,000.00, or over in addition to which the usual deduction for charges abroad, foreign government stamps, etc., is made.

472 *Claimant's Exhibit 1.*
*Claimant's Exhibit 2.*

Our extensive connections assure prompt and efficient service, especially for collections in Continental Europe where we have specialized with a view to meeting every requirement of our correspondents.

(Note, Pages 13-82 of Claimant's Exhibit 1 contain lists of foreign banks which might be drawn on pursuant to the "Terms and Conditions" set forth in pages 1-12 of the Exhibit. A complete copy of the original Exhibit will be produced at
473 the argument).

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**Claimant's Exhibit 2.**

(Note.—This Exhibit was a book of forms of drafts and advices. A paper label on its cover reads as follows):

FOREIGN DRAFTS

From No..... to No.....

The Terms and Conditions under which our correspondents may use the within forms are contained in our list of foreign correspondents, and are subject to change
474 by us from time to time.

Upon receipt of advice of draft accompanied by adequate funds payable at par in New York, we shall promptly forward our advice of same, and make provision for its payment abroad, provided it is drawn on a bank named in our latest list of correspondents.

Under this arrangement our correspondents draw drafts for their own account as principals and our name does not appear, our sole function

being to advise the drawees of the issue of drafts drawn by our correspondents and to provide for payment, in which function we act as agents of the drawers.

To secure prompt payment of drafts, our correspondents must mail their advices and remittances to us on the day such drafts are issued.

Further information and instructions are contained in our latest list of foreign correspondents the provisions of which are hereby referred to and made a part hereof. The use of our facilities will be considered as acceptance of our conditions.

Covering remittances to us should be in exchange on New York, unless otherwise arranged, and must be strictly in accordance with our rates, as issued from time to time, and are subject to the provisions under which our rate quotations are made.

If a remittance be made at a wrong rate, we may return same or hold it and advise the remitter of the shortage or excess; or we may advise the draft abroad and require payment to us of the shortage or return the excess to our correspondent, as the case may be.

KNAUTH, NACHOD & KUHNE
New York.

(Note. A typical set of forms as contained in Claimant's Exhibit 2 is set forth on the following page.)

478

*Claimant's Exhibit 2.*

RECEIPT FOR THE SALE OF

Trinidad, Colo.,

Draft No..... Date.....
Sold to .....
.....
Drawn on .....
.....
Order of .....
Foreign Amount .....
Rate..... Am't Rec'd $.....

We would suggest the advisability of registering the letter in which the draft is mailed abroad.

479

THE FIRST NATIONAL BANK
of
Trinidad, Colo.

THE FIRST NATIONAL BANK
of
Trinidad, Colo.

No..... Trinidad, Colo.,

CHECK FOR

..... .....192...

Duplicate Unpaid

Pay from balance against this CHECK to

.....or order
.....
.....

THE FIRST NATIONAL BANK OF TRINIDAD

To.....
.....
.....
.....

ISSUING BANK'S RECORD

Draft No..... Date.....

Sold to .....
.....
Drawn on .....
480 .....

Order of .....

Foreign Amount .....

Rate..... Am't Rec'd $.....

In order to lessen the possibility of error drafts should be prepared on the typewriter.

Paid K N & K.....
(Transfer Agents)
Profit $ .....

No.

Advice to be mailed immediately to K. N. & K. Bank Delivery, New York with N. Y. Funds to cover.

Pursuant to the terms and conditions governing your drawing service we have sold draft, bearing the above number, dated,

Trinidad, Colo.....192...

For.....and shall thank you to protect same upon presentation.

We remit herewith the sum of $.....@ Rate.....

Quoted { On Rate Card No. / in Telegram of / Telephone from } .....

For K. N. & K.
Rate Checked
Extension Checked

Payee .....

Amount .....

THE FIRST NATIONAL BANK OF TRINIDAD

Drawn on .....
.....
.....
.....

THE FIRST NATIONAL BANK
OF
TRINIDAD, COLO.

**Claimant's Exhibit 3.** 481

No. 61161

Trinidad, Colo.
May 19th, 1923
Duplicate unpaid

Check for
Lit. 24,360.00

Pay from balance against this Check to Zara Sanna Giovanni or order Twenty four thousand, three hundred Sixty and 00/100 Lire.

To Banca Commerciale Italiana.
Sassari-Italia.

THE FIRST NATIONAL BANK OF TRINIDAD
S. MONE,
Cashier. 482

**Claimant's Exhibit 4.**

Advice to be mailed immediately to K. N. & K., bank delievery, New York, with N. Y. funds to cover.

No. 61161

8469 B 69 B

Pursuant to the terms and conditions governing your drawing service we have sold draft, bearing the above number, dated, Trinidad, Colo., May 19, 1923.

For Lit. 24,360.00 and shall thank you to protect same upon presentation.

We remit herewith the sum of $1,191.20 @ rate 483

4.89 quoted { on Rate Card No. / in Telegram of / Telephone from } 18

Payee Zara Sanna Giovanni.

Amount Twenty four thousand, three hundred Sixty Lire.

Drawn on Banca Commerciale Italiane,
Sassari,
Italia.

THE FIRST NATIONAL BANK OF TRINIDAD
S. MONE,
Cashier.

Founded 1852
K N & K
New York
Advice of drafts drawn

When referring to drafts below please mention this number.
S. S. No. 8469-B
Date May 22, 1923.

Banca Commerciale Italiana
Genoa
Italia

| Number | Issued by | City | Date | In favor of | Lire |
|---|---|---|---|---|---|
| 686029 | Union Svgs Bank & Tr Co | S Eubenville O | May 21. | Passadore & Co | 15.000.00 |
| 89800 | Ourselves | New York | May 22. | A. Gannu | 4.350.00 |
| | | | | | 19.350.00 |
| 93194 | " | " | " | Banca Comm. Italiana A-C First Italian St Bank Chicago Ill. | 50.000.00 |
| | | | | | 69.350.00 |

Please honor the above listed drafts charging same to our account

Very truly yours,
KNAUTH, NACHOD & KUHNE.
By H. B. Duncan-Clarke

Form A-3

**Claimant's Exhibit 6-B.**

493

Founded 1852
K N & K
New York
Advice of drafts drawn

When referring to drafts below please mention this number.
S. S. No. 8469-B
Date May 22, 1923.

Banca Popalare Di
Ascoli Piceno Italia

| Number | Issued by | City | Date | In favor of | Lire |
|---|---|---|---|---|---|
| 705866 | The Sec Svgs Bank & Tr Co | Toledo O | May 19 | Agostino Alesi | 5,500.00 |

494

Please honor the above listed drafts charging same to our account with Banca Comm. Italiana Genoa

Very truly yours,

KNAUTH, NACHOD & KUHNE.
By H. B. Duncan-Clarke

Form A-3

495

Founded 1852
K N & K
New York
Advice of drafts drawn

When referring to drafts below please mention this number.
S. S. No. 8469-B
Date May 22, 1923.

Banca Commerciale Italiana
Caltanissetta Italia

| Number | Issued by | City | Date | In favor of | Lire |
|---|---|---|---|---|---|
| 685944 | First Nat Bank | Hazelton Pa | May 21. | Alsoldata Pane Angelino Compagnia Distrettuale | 50.00 |
| 655268 | Rochester Tr & Safe Dep Co | Rochester N. Y. | May 21. | Dominicelli Antonio | 1.000.00 |
| | | | | | 1.050.00 |

Please honor the above listed drafts charging same to our account with Banca Comm. Italia Genoa

Very truly yours,

KNAUTH, NACHOD & KUHNE.
By H. B. Duncan-Clarke

Form A-3

Founded 1852
K N & K
New York
Advice of drafts drawn

When referring to drafts below
please mention this number.
S. S. No. 8469-B
Date May 22, 1923.

Banca Commerciale Italiana
Sassari
Italia

| Number | Issued by | City | Date | In favor of | Lire |
|---|---|---|---|---|---|
| 61160 | The First Nat Bank | Trinidad Colo | May 19 | Sassu Mebelle Vittoria | 14.210.00 |
| 61161 | " | " | " | Zara Sanna Giovanni | 24.360.00 |
| | | | | | 38.570.00 |

Please honor the above listed drafts charging same to our account with Banca Comm. Italiana Genoa

Very truly yours,

KNAUTH, NACHOD & KUHNE.
By H. B. Duncan-Clarke

Form A-3

501

500

499

Claimant's Exhibit C-D.

167

Founded 1852
K N & K
New York
Advice of drafts drawn

When referring to drafts below please mention this number.
S. S. No. 8469-B
Date May 22, 1923.

Banca Commerciale Italiana
Roma
Italia

| Number | Issued by | City | Date | In favor of | Lire |
|---|---|---|---|---|---|
| 637518 | The Peoples Bank | Buffalo N. Y. | May 21. | Felix Mc Cabe | 610.00 |
| 89785 | Ourselves | New York | May 22. | Ministero Delle Poste E Dei Telegrafi Original only | 9.280.20 |
| | | | | | 9.890.20 |
| 89799 | " | " | " | A. Gannuscio | 15.650.20 |
| 93189 | " | " | " | Ministero Delle Poste E Dei Telegrafi | 57.498.20 |
| | | | | | 83.038.60 |

Please honor the above listed drafts charging same to our account with Banca Comm. Italiana Genoa

Very truly yours,

KNAUTH, NACHOD & KUHNE.
By H. B. Duncan-Clarke

Form A-3

Claimant's Exhibit 6-E.

| Dare 1923 | | Causale | |
|---|---|---|---|
| Maggio | 28 | bonifico Pittsburgh St Bk | ..... |
| | " | spere | ..... |
| | " | " | ..... |
| | 29 | " | Velig ..... |
| | 31 | " | ..... |
| | " | disp. 89688 | ..... |
| | " | " | ..... |
| Fiuguo | 1 | " list 8464.B. | ..... |
| | " | " " — 5.B. | ..... |
| | " | " " — 6.A. | ..... |
| | " | " " — 5.A. | ..... |
| | " | " " — 4.A. | ..... |
| | " | " " — 6.B. | ..... |
| | " | " " — 8.B. | ..... |
| | " | " " — 8.A. | ..... |
| | " | " " — 8.C. | ..... |
| | " | spere | ..... |
| | " | bonifico D. M. fiuli | ..... |
| | " | " | ..... |
| | " | disp. list 8467 A. | ..... |
| | " | " | ..... |
| | " | " | ..... |

A riportar

Giuguo 2 Saldo Creditore .....

Avere

Riporto ..

**Claimant's Exhibit 7.**

505

AUTH NACHOD & KUHNE Loro Conto ordinario colla BANCA COMMERCIALE ITALIANA— Sede di Geno
New York al 2 Fiuguo 1923

Pagamento al nostro domicilio.

| | Importo | Valuta | 1923 | | Causale | | Importo | Avere Valuta |
|---|---|---|---|---|---|---|---|---|
| Riporto | Lt 45,933,472.78 | | | | | Riporto ..... Lit. | 46,128,089.34 | |
| ..... | 100,000.— | Maggio | 28 Maggio | 31 | verof. Credito of spede N. Y. ..... | | 250,000.— | Maggio 31 |
| ..... | 1.— | | " | " | " " " Hallgarten ..... | | 250,000.— | 31 |
| ..... | 1.— | | " | " | " Merithea of East River ..... | | 500,000.— | 31 |
| ..... | 43.50 | | " Fiuguo | 1 | " Bea Natz del Reduce giu p. v. c..... | | 250,000.— | 22 |
| ..... | —.90 | | " | " | " " " " " " " " " ..... | | 250,000.— | 28 |
| ..... | 50,000.— | | 30 | " | " Credito of French Am. Bk. S. Tran. ..... | | 200,000.— | Fiuguo 1 |
| ..... | 1.— | | " | | | | | |
| ..... | 81,637.40 | | 29 | | | A riportare ..... Lit. | 47,828,089.34 | |
| ..... | 111,221.20 | | 29 | | | | | |
| ..... | 131,791.— | | 29 | | | | | 506 |
| ..... | 75,000.40 | | 29 | | | | | |
| ..... | 2,118.— | | 29 | | | | | |
| ..... | 187,950.10 | | 29 | | | | | |
| ..... | 116,680.40 | | 31 | | | | | |
| ..... | 49,745.— | | 31 | | | | | |
| ..... | 325,000.40 | | 31 | | | | | |
| ..... | 63.80 | | " | | | | | |
| ..... | 100,000.— | Fiuguo | 1 | | | | | |
| ..... | 5.55 | | " | | | | | |
| ..... | 25,300.— | | 1 | | | | | |
| ..... | —.50 | | " | | | | | |
| ..... | —.30 | | " | | | | | |
| ..... | Lit. 47,290,034.23 | | | | | | | |
| ..... | 538,055.11 | | | | | | | |
| | Lit. 47,828,089.34 | | | | | | | 507 |
| ..... | Lit. 47,828,089.34 | | | | | | | |
| | Lit. 47,828,089.34 | | Fiuguo | 2 | Saldo Precedente ..... | Lit. | 538,055.11 | Diverse |

508 **Claimant's Exhibit 8.**

SIGG. KNAUTH NACHOD & KUHNE Loro Conto ordinario colla BANCA COMMERCIALE ITAL
New York al 9 Fiuguo

Pagamento al nostro domicilio

| DARE 1923 | | Causale | Importo | Valuta 1923 | | Causale |
|---|---|---|---|---|---|---|
| | | Riporto ..... | Lit. 47,290,034.23 | | | |
| fiuguo | 4 | spere ..... | 1.80 | fiuguo | 4 | verol. Bca Naz di Credito |
| | " | disp. list 8470 A. ..... | 100,000.— | fiuguo | 1 | " " Bca di Roma of sp |
| | " | " " 8469 A. ..... | 44,100.— | | 2 | " " " " " " " " |
| | " | " " 8469 B. ..... | 197,508.60 | | 2 | " " Wers Banca of Ea |
| | " | " ..... | 12.90 | | 3 | " " Credito op Nat Bk |
| | " | pag. Bca Naz Di Credito of Italdisco..... | 250,000.— | | 4 | " " " " Equit. |
| | " | spere ..... | —.30 | " | | 5 " Bca Nat. del Redu |
| | 5 | " ..... | —.30 | " | | 6 Credito of Equi Trust |
| 509 | 6 | disp. list 8471 B. ..... | 75,400.— | | 6 | " disp. 420,049 anem Uata |
| | " | " ..... | 2.70 | " | | " verof. Credito of Intern |
| | " | bonifico Fourth Atlantic—Boston ..... | 250,000.— | | 6 | " " " of Chase Na |
| | " | " Bca Popolare Fugaj.—S. Francisco ..... | 250,000.— | | 6 | |
| | " | " F. Buty & C. Seattle ..... | 100,000.— | | 6 | |
| | " | spere ..... | —.30 | " | | |
| | " | disp. list 8472 A. ..... | 304,700.20 | | 6 | |
| | " | " ..... | 3.70 | " | | |
| | " | " ..... | 1.— | " | | |
| | " | " ..... | —.30 | " | | |
| | " | " 93232 ..... | 10,000.— | | 6 | |
| | " | " 93257 ..... | 250,000.— | | 6 | |
| | " | " " 8471 A. ..... | 79,600.20 | | 6 | |
| | " | " " 8472 A. ..... | 20,000.20 | | 6 | |
| | " | " ..... | 1.50 | " | | |
| | " | " ..... | —.30 | " | | |
| 510 | 7 | " ..... | 2.— | " | | |
| | | A riportare ..... | L. 49,221,370.53 | | | |

Rec'd Jun 25 1923
Ans'd

...ERCIALE ITALIANA—Sede di Genoa
...al 9 Fiuguo 1923

| ...ale | | Importo | Avere Valuta |
|---|---|---|---|
| | Riporto ..... Lit. | 47,828,089.34 | |
| ...z di Credito of. Italiano..... | | 150,000.— | fiuguo 4 |
| ...Roma of spede Firuye ..... | | 150,000.— | 4 |
| " " " Roma ..... | | 250,000.— | 4 |
| ...anca of East River ..... | | 250,000.— | 4 |
| ...op Nat Bk of Comm. N. Y. ..... | | 250,000.— | 4 |
| " Equit. Trust N. Y..... | | 250,000.— | 4 |
| ...t. del Reduce of spede N. Y..... | | 250,000.— | 4 |
| ...qui Trust ..... | | 250,000.— | 6 |
| ...anem Uata ..... | | 6,600.— | 6 |
| ...o of Intern. Accept. Bk. N. Y..... | | 250,000.— | 6 |
| ...of Chase Nat Bk N. Y..... | | 500,000.— | 6 |

A riportare ..... Lit. 50,384,689.34

*Claimant's Exhibit 8.*

| | | | |
|---|---|---|---|
| | Riporto ..... | Lit. 49,221,370.53 | |
| fiuguo 7 | disp. list 8475 A. ..... | 60,000.20 | |
| " | " " 8474 B. ..... | 34,200.20 | |
| " | spere..... | 1.— | |
| " | Pay Credito op. Guaranty N. Y. ..... | 250,000.— | |
| " | ..... | —.30 | |
| " | disp. list 8470 B. ..... | 110,055.— | |
| " | " " 8470 A. ..... | 7,781.— | |
| " | " " 8474 C. ..... | 294,400.40 | |
| " | " " 8474 A. ..... | 19,586.— | |
| " | " ..... | 56.30 | |
| " | " ..... | —.30 | |
| " | bonifico Pittsburgh St. Bk.—Pittsburgh..... | 100,000.— | |
| " | spere ..... | 1.— | |
| " | " ..... | 8.— | |
| 9 | " ..... | —.30 | |
| " | " ..... | 1.— | |
| " | Saldo Creditore ..... | 688,242.81 | |
| | | Lt 50,785,704.34 | |

| | | | |
|---|---|---|---|
| fiuguo 7 | fiuguo 8 | verof. Credito op. French | |
| 7 | 9 | " Merit banca of East | |
| " | " | disp. 56925 anneltata .... | |
| 7 | | | |
| " | | | |
| 6 | | | |
| 6 | fiuguo 9 | Saldo Precedente ..... | |
| 7 | | | |
| 7 | | | |
| " | | | |
| " | | | |
| 8 | | | |
| " | | | |
| " | | | |
| " | | | |
| " | | | |

S. E. & O.
Genova li *9. fiuguo 1921*

*Claimant's Exhibit 8.*

511

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| ..... | Lit. 49,221,370.53 | | | Riporto ..... | Lit. 50,384,689.34 | | |
| ..... | 60,000.20 | fiuguo 7 | fiuguo 8 | verof. Credito op. French American S. Francisco ..... | 150,000.— | fiuguo 8 | |
| ..... | 34,200.20 | 7 | 9 | " Merit banca of East River N. Y..... | 250,000.— | 9 | |
| ..... | 1.— | " | " | disp. 56925 anneltata ..... | 1,015.— | 9 | |
| ..... | 250,000.— | 7 | | | | | |
| ..... | —.30 | " | | | Lit. 50,785,704.34 | | |
| ..... | 110,055.— | 6 | | | | | |
| ..... | 7,781.— | 6 | fiuguo 9 | Saldo Precedente ..... | Lit. 688,242.81 | Diverse | |
| ..... | 294,400.40 | 7 | | | | | |
| ..... | 19,586.— | 7 | | | | | |
| ..... | 56.30 | " | | | | | |
| ..... | —.30 | " | | | | | |
| ..... | 100,000.— | 8 | | | | | |
| ..... | 1.— | " | | | | | |
| ..... | 8.— | " | | | | | 512 |
| ..... | —.30 | " | | | | | |
| ..... | 1.— | " | | | | | |
| ..... | 688,242.81 | | | | | | |
| | Lit 50,785,704.34 | | | | | | |

S. E. & O.
Genova li *9. fiuguo 1921*

513

**Claimant's Exhibit 9.**

nario colla Banca Commerciale Italiana — Sede di Genova
al 16 fuiguo

Rec'd Jul 5 1923
Ans'd

| Importo | Valuta | | 1923 | | Pagamento al nostro Domicilio. Causale | Importo | Avere Valuta | |
|---|---|---|---|---|---|---|---|---|
| Lit. 50,097,451.53 | | | | | Riporto Lit. | 50,785,704.34 | | |
| 50.000.— | fiuguo | 11 | fiuguo | 11 | versf. Credito of Nat. Shwament Boston | 250,000.— | fiuguo | 11 |
| .30 | " | " | | 12 | if umeng incanata | 149,998.80 | | 13 |
| 42.— | " | " | | 15 | versf. Credito of Richard | 140,000.— | | 15 |
| 43,100.— | | 11 | | 16 | " Beg Nat del Reduce of. sperte N. Y. | 500,000.— | | 16 |
| 118,500.80 | | 11 | | | | | | |
| 5.30 | | " | | | | | | |
| 84,826.20 | | 11 | | | | | | |
| 3.70 | | " | | | | | | |
| 1.20 | | " | | | | | | |
| 70,978.90 | | 11 | | | | | | |
| 124,642.20 | | 11 | | | | | | |
| 8.40 | | " | | | | | | |
| 71,285.— | | 11 | | | | | | |
| 34,300.— | | 11 | | | | | | |
| 11.35 | | " | | | | | | |
| 1.— | | " | | | | | | |
| 250,000.— | | 13 | | | | | | |
| .30 | | " | | | | | | |
| 7,894.— | | 15 | | | | | | |
| 5.30 | | " | | | | | | |
| .30 | | " | | | | | | |
| 77.50 | | " | | | | | | |
| 93,894.— | | 14 | | | | | | |
| 48,552.— | | 14 | | | | | | |
| 463,468.60 | | 14 | | | | | | |
| Lit. 51,559,079.88 | | | | | /riportare Lit. | 51,825,703.14 | | |

514

**Claimant's Exhibit 9.**

Sigg. Knauth Nachod & Kuhne Loro Conto Ordinario colla Banca Commerciale Italiana — Sede di Genova
New York al 16 fuiguo

Dare

| 1923 | Causale | Importo | Valuta |
|---|---|---|---|
| | Riporto..... Lit. | 50,097,451.53 | |
| fuiguo 11 | disp 90219 ..... | 50.000.— | fiuguo 11 |
| " | spere ..... | .30 | " " |
| " | " Telig ..... | 42.— | " " |
| " | " list 8475 A. ..... | 43,100.— | 11 |
| " | " " 8475 B. ..... | 118,500.80 | 11 |
| " | " ..... | 5.30 | " |
| 515 12 | " " 8476-B. ..... | 84,826.20 | 11 |
| " | " ..... | 3.70 | " |
| " | " ..... | 1.— | " |
| " | " " 8476 C. ..... | 70,978.— | 11 |
| " | " " 8477 B. ..... | 124,642.20 | 11 |
| " | " ..... | 8.40 | " |
| " | " " 8470 A. ..... | 71,395.— | 11 |
| " | " " 8477 A. ..... | 34,300.— | 11 |
| " | " ..... | 11.35 | " |
| " | " ..... | 1.— | " |
| 13 | pag. credito I. Richard ..... | 250,000.— | 13 |
| " | spere ..... | .30 | " |
| 15 | disp. 8478 A. ..... | 7,804.— | 15 |
| " | " ..... | 5.30 | " |
| " | " ..... | .30 | " |
| " | Telig ..... | 77.50 | " |
| 516 16 | " 8479 B. ..... | 93,894.— | 14 |
| " | " 8479 A. ..... | 48,552.— | 14 |
| " | " 8479 C. ..... | 463,468.60 | 14 |
| | A riportare Lit. | 51,559,079.88 | |

Pagamento al nostro Domic

| 1923 | Causale |
|---|---|
| fiuguo 11 | versf. Credito of Nat. Sh |
| 12 | if umeng incana |
| 15 | versf. Credito of Richar |
| 16 " | Beg Nat del Redi |

*Claimant's Exhibit 9.*

| | | | |
|---|---|---|---|
| | Riporto..... | Lit. 51,559,079.88 | |
| fuiguo 16 | disp 8481 A. ..... | 16,780.— | fiuguo 15 |
| " | spere ..... | 19.30 | " |
| " | " 8480 A. ..... | 8,837.— | 16 |
| " | " 8480 B. ..... | 153,525.80 | 16 |
| " | " ..... | 18.60 | " |
| " | " Telig ..... | 91.30 | " |
| " | Saldo Creditore ..... | 87,351.26 | |
| | | Lit. 51,825,703.14 | |

fiuguo 16 Saldo Precedente ..

S. E. & O.

Genova li 16-6-25

*Claimant's Exhibit 9.*

517

| | | |
|---|---|---|
| .....Lit. | 51,559,079.88 | |
| ..... | 16,780.— | fiuguo 15 |
| ..... | 19.30 | " |
| ..... | 8,837.— | 16 |
| ..... | 153,525.80 | 16 |
| ..... | 18.60 | " |
| ..... | 91.30 | " |
| ..... | 87,351.26 | |
| Lit. | 51,825,703.14 | |

Riporto Lit. 51,825,703.14

Lit. 51,825,703.14

fiuguo 16 Saldo Precedente ..... Lit. 87,351.25 diverse

S. E. & O.

Genova li 16-6-25

518

519

520

**Claimant's Exhibit 10.**

*Cablegram.*

Date June 16, 1923

To Banca Commerciale Italiana
Genoa, Italy

U. S. Court to-day appointed Middleton S. Borland Receiver of our firm, Knauth, Nachod & Kuhne. I have to-day taken possession all assets of K., N. & K., New York. All credit balances in favor of K., N. & K., New York
521 must be held subject to my sole order.

Yours very truly,

Middleton S. Borland
Receiver.

BK-AB
Form 18-B—1000-4.23

175

522

**Claimant's Exhibit 11.** 523

BANCA COMMERCIALE ITALIANA

Societa Anonima-Sede in Milano

Capitale Sociale L400,000,000

Versato $348.786.000 Riserve L176.000.000

Sede Di Genova

Rec'd Jul 5, 1923
Ans'd

Codici Telegrafici
A B C 4.a & 5.a edizone
Liebers Standard & 5-Letter Code
Western Union
A Z francais 524
Century Standard
Peterson's Int. Banking Code
Bentley's Complete Phrase Code

Segreteria B.

GENOA, June 22nd, 1923.

MIDDLETON S. BORLAND, ESQ.,
Receiver of Messrs. Knauth, Nachod & Kuhne,
NEW YORK.

DEAR SIR

We have to acknowledge receipt of your cablegram of the 16th inst. reading:

> "United States Court today appointed 525
> Middleton S. Borland receiver of our firm Knauth Nachod & Kuhne stop I have today taken possession all assets of Knauth Nachod & Kuhne stop All credit balances in favour of Knauth Nachod & Kuhne of New York must be held subject to my sole order"

Telegrammi: Comitbanca Genova Lettera di Conto Corrente
Tutti i fogli componenti questa lettera devono essere firmati.

526 *Claimant's Exhibit 11.*

of which we have taken due note, and, in order to comply with our general requirements, should esteem it a favour if you would forward us a copy of the receiving order issued by the U. S. Court wherein your appointment was made.

We enclose herewith a statement of the account of Messrs. Knauth, Nachod & Kuhne as at the close of business on the 16th. inst. showing, in principal only, a balance in their favour of:

Lit. 87.351,26.—from which is to be deducted an approximate sum of:

" 8.954,00.—debit balance Dollars Account

527 ($407.15)

" 78.397,26.—

On the 18th. inst. we debited you with:

Lit. 1.—for postage expenses, and now credit you with:

Lit. 158,00—value today, June 22nd, in cancellation of draft No. 8284/34308 drawn by First Nat. Bank, Shreveport, on Banca di Sicilia, Cefalo;

Lit. 12,500.00—value today, in cancellation of drafts Nos. 8450/89135 and 8450/89171 drawn by K. N. & K. on us;

Lit. 60.00—value today, in cancellation of draft

528 No. 8476/733906 drawn by Liberty Sav. Bk. & Trust Co., Memphis, on our Alessandria Branch.

During the last few days several drafts already debited in account have been presented, payment of which we have refused, and would ask you to inform us by CABLE whether we are to pay drafts which have already been passed to the debit of the account or whether we are to consider them as cancelled and re-credit them to the account of Messrs. Knauth, Nachod & Kuhne.

We would ask you further to note that the following orders are being held in abeyance, not

Telegrammi: Comitbanca Genova
Tutti i fogli componenti questa lettera devono essere firmati.

having been debited to the account through lack of funds:

Lit. 300.000.—transfer in favour of Pittsburgh State Bank, Pittsburgh ...as per cable 11/6

" 100.000.—transfer in favour of D. M. Giuli & Son, Milwaukee .....as per cable 11/6

" 100.000.—transfer in favour of Mellon National Bank, Pitsburgh ...as per cable 12/6

" 100.000.—transfer in favour of Pittsubrgh State Bank, Pittsburgh ...as per cable 14/6

Lit. 500.000.—transfer in favour of Banca Popolare Fugazi, S. Francisco .....as per cable 15/6

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| it. | 17.000.— | drafts— | List | No. | 8481 B— | as per | mail | advice | | 6/6 |
| " | 129.560.60 | " | — | " | " | 8482 A— | " | " | " | " | 7/6 |
| " | 327.518.00 | " | — | " | " | 8482 B— | " | " | " | " | 7/6 |
| " | 89,500.00 | " | — | " | " | 8483 A— | " | " | " | " | 8/6 |
| " | 97.418.20 | " | — | " | " | 8483 B— | " | " | " | " | 8/6 |
| " | 10.000.20 | " | — | " | " | 8484 A— | " | " | " | " | 9/6 |
| " | 871.50 | " | — | " | " | 8484 B— | " | " | " | " | 9/6 |
| " | 75.650.40 | " | — | " | " | 8485 A— | " | " | " | " | 11/6 |
| " | 41.000.00 | " | — | " | " | 8485 B— | " | " | " | " | 11/6 |
| " | 221.039.00 | " | — | " | " | 8485 C— | " | " | " | " | 11/6 |

In safe custody we hold:

Lit. 24.600.—(nominal value) "Rendita Italiana" (Console) 3½% registered in the name of Raffo Colomba, as per enclosed description, (see our last letter to K. N. & K., dated 23/4/23. P. A. 825), and should be glad to have your authorization to

52

530

531

Telegrammi: Comitbanca Genova
Tutti i fogli componenti questa lettera devono essere firmati.

532 *Claimant's Exhibit 11.*
*Claimant's Exhibit 12.*

deliver these securities to the interested parties, whose address we would ask you at the same time to indicate.

We await the favour of your early reply, and beg to remain, Dear Sir, Yours very truly,

BANCA COMMERCIALE ITALIANA.

Sede di Genova.

Encl: Statement.
Description of
securities in safe custody.

533

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**Claimant's Exhibit 12.**

*Cablegram.*

JUNE 26, 1923.

BANCA COMMERCIALE ITALIANA
Genoa, Italy

Please purchase Dollars for equivalent all ballances and cable proceeds Central Union Trust Company, New York, for credit Middleton S. Borland, Receiver for Knauth, Nachod & Kuhne, New
534 York. Cable result.

MIDDLETON S. BORLAND,
Receiver.

**Claimant's Exhibit 18.** 535

Receiver for
INFORMATION COPY
CABLEGRAM RECEIVED

Date June 30th, 1923.

From
BANCA COMMERCIALE ITALIANA
Genoa, Italy

Dated.....

received here today as follows:

Refer to your cablegram of 26th. cannot make any reimbursement before we know position all our branches. On receipt of our letter of June 22nd reply by cable. 536

Yours very truly,

4 C. I.—10M—11,22.

**Claimant's Exhibit 14.**

JUNE 29, 1923.

BANCA COMMERCIALE ITALIANA,
Genoa, Italy.

DEAR SIRS:

Enclosed you will find court order appointing me Receiver for Knauth, Nachod & Kuhne, New York, certified to by your Consulate here. 537

I confirm my cable of June 26th reading as follows:

"Please purchase Dollars for equivalent all balances and cable proceeds Central Union Trust Company, New York, for credit Middleton S. Borland, Receiver for Knauth, Nachod & Kuhne, New York. Cable result. Middleton S. Borland, Receiver."

538 *Claimant's Exhibit* 14.

I request you to kindly rule off the account of Knauth, Nachod & Kuhne on the day on which my first cable (confirmation enclosed) informing you of the Receivership reached you, and to forward to me by return mail a statement of their account up to that date, as well as a list of all unexecuted cable transfers and unpaid drafts and money orders, sating the numbers of reports in which the items were advised by Knauth, Nachod & Kuhne.

Yours very truly,

539 MIDDLETON S. BORLAND, Receiver.

M. F.

Encls.

540

**Claimant's Exhibit 15.** 541

BANCA COMMERCIALE ITALIANA

Societa Anonima—Sede in Milano

Capitale Sociale L400.000.00 Versato L348.786.000 Riserve L176.000.00

Sede di Genova

Telegrafici Codici
- A B C 4.a & 5.a edizone
- Liebers Standard & 5, Letter Code
- Western Union
- A Z francais
- Century Standard
- Peterson's Int. Banking Code
- Bentley's Complete Phrase Code

542

Segreteria B.

GENOA, July 12th, 1923.

MIDDLETON S. BORLAND, ESQ.,
Receiver for Messrs. Knauth, Nachod & Kuhne,
NEW YORK.

DEAR SIR,

We have to thank you for your favour of the 29th. ult. with which you forward us a copy of the court order appointing you Receiver for Knauth, Nachod & Kuhne, New York, duly certified by the Italian Consul in New York.

With regard to your cable of the 26th. ult. reading: 543

> "Please purchase Dollars for equivalent all balances and cable proceeds Central Union Trust Company, New York, for credit Middleton S. Borland, Receiver for Knauth Nachod & Kuhne New York. Cable result"

we have to confirm our wire of the 29th. ult.:

"Refer to your cablegram of 26th. can-

Telegrammi: Comitbanca Genova Lettera Di Conto Corrente
Tutti i fogli componenti questa lettera devono essere firmati

544 *Claimant's Exhibit 15.*

not make any reimbursement before we know position all our Branches stop On receipt of our letter of June 22nd. reply by cable"

so that, while we have got into immediate communication with all our Branches on receipt of your first telegram, we are not yet fully posted as to the position of all.

We would further refer you to our letter of June 22nd. in which we desired you to advise us by CABLE whether we are to pay drafts which have already been passed to the debit of the account
545 or whether we are to consider them as cancelled and to re-credit them to the account of Messrs. K. N. & K.

As we are up to the time of writing without your reply on this point, we have, in view of numerous requests which we are receiving, wired you today as follows:

"Refer to our letter of 22nd. to our cablegram of 29th. June please cable whether we may pay all drafts already charged to the account of Knauth, Nachod & Kuhne, New York"

546 to which we trust to have your prompt response enabling us to regulate this matter.

We take leave to debit the account of K. N. & K with: Lit. 157.55—cable expenses (85.30 and 72.25) and beg to remain, Dear Sir,

Yours very truly,

BANCA COMMERCIALE ITALIANA.
Sede di Genova.

Telegrammi: Comitbanca Genova
Tutti i fogli componenti questa lettera devono essere firmati

547

**Claimant's Exhibit 16.**

Receiver for

ACTION COPY

CABLEGRAM RECEIVED

Date JULY 13, 1923
General File
Cable Dept.
By B. K.

From
BANCA COMMERCIALE ITALIANA
Genoa, Italy

548

Dated.....

received here today as follows:

Refer to our letter of 22nd (of June) refer to our cablegram of 29th (of June) June please cable whether we may pay all drafts already charged to the account of K., N. & K., New York.

Yours very truly,

549

**Claimant's Exhibit 17.**

*Cablegram.*

Date JULY 13, 1923

To

BANCA COMMERCIALE ITALIANA
Genoa, Italy

Answering your cable message I reaffirm our cable message of June 16th. Nothing should be paid or charged Knauth, Nachod & Kuhne, New York, after June 16th irrespective date advised or charged. All drafts charged but not paid must be recredited and balance must be sold and remitted by wire without further delay, as per our wire of June 26th.

Yours very truly,

MIDDLETON S. BORLAND
Receiver.

BK—A B
Form 18B.—10000—4-23

**Claimant's Exhibit 18.**

*Cablegram.*

Date AUGUST 23, 1923

To

BANCA COMMERCIALE ITALIANA
Genoa, Italy

Refer to your letter of July 12th please cancel all drafts charged but not paid before Receivership and remit balance for (our) my credit to Central Union Trust Co., New York.

Yours very truly,

MIDDLETON S. BORLAND
Receiver.

MS—TWK
Form 18B.—10000—4-23

**Claimant's Exhibit 19.**

553

Rec'd Sep 26 1923
Ans'd

BANCA COMMERCIALE ITALIANA

Societa Anonima—Sede in Milano

Capitale Sociale L.400.000.000

Versato L.348.786.000 Riserve L.176.000.000

**Sede di Genova**

Codici Segreteria A
- Telegrafici
- A B C 4.a & 5.a edizone
- Liebers Standard & 5, Letter Code
- Western Union
- A Z francais
- Century Standard
- Peterson's Int. Banking Code
- Bentley's Complete Phrase Code

554

GENOA, September 10th, 1923.

MIDDLETON S. BORLAND, Esq.,
Receiver for Messrs. Knauth, Nachod & Kuhne,
New York.

DEAR SIR,

We beg to confirm our letter of the 8th. inst. and to acknowledge receipt of your cablegram of the 23rd. ult. reading:

555

> "Refer to your letter of July 12th. please cancel all drafts charged but not paid before receivership and remit balance for our credit to Central Union Trust Co., New York."

Information has now been received from all our Branches regarding unpaid drafts and we enclose herewith statement of drafts which had been debited but not paid prior to the appointment of the receivership.

We are crediting the sum of:

Telegrammi: Comitbanca Genova Lettera Di Conto Corrente
Tutti i fogli componenti questa lettera devono essere firmati

*Claimant's Exhibit 19.*

Telegrammi: Comitbanca Genova
Tutti i fogli componenti questa lettera devono essere firmati

Lit. 1.526.048.48.—value September 10th, 1923, to the account of Messrs. Knauth, Nachod & Kuhne, and:
$300.— value September 10th, 1923 to their Dollars Account.

You will further find enclosed herewith statements of the Lire and Dollar Accounts, closed at today's date, showing the following balances:
Lit. 1.629.770.00.—in your favour, from which must be deducted:

$ 115.—balance of our Dollar Account in our favour.

557 $4000.—value March 5th., balance due to our Milan Office in their Dollar Account.
as also such sum as may be due to our New York in their Dollar Account with Messrs. K. N. & K.

Consequently, we have today passed telegraphic instructions to our New York Agency to pay you the sum of:

Lit. 1.629.770.00 —less
Lit. 220.00.—our cable expenses, viz:
Lit. 1.629.550.00.—after deducting from this amount:

558 $115 and $4000.—as stated above, together with such amount as may be due to them.

We would thank you to acknowledge receipt of the enclosed lists and also to let us know when the enclosed statements have been found correct.

We are, Dear Sir,

Yours very truly,
Banca Commerciale Italiana,
Sede di Genova.

Encl: List of unpaid drafts.
3 Statements (2 Dollar &
1 Lire)

## Claimant's Exhibit 19A.

559

MESSRS. KNAUTH, NACHOD & KUHNE—UNPAID DRAFTS.

| Issued by | Issued on | | Amount | List No. | List dated |
|---|---|---|---|---|---|
| | | | 1.174.098,08 | | |
| Nat. Bk—Los Angeles | Our Roma Office | Lit | 600,— | | |
| Trust Co—N. Kesing | id. | " | 2.000,20 | | |
| Bk Buffalo—New York | id. | " | 192,— | | |
| id. | id. | " | 610,— | | |
| id. | Our Torino Office | " | 2.222,— | | |
| Bk—Rochester | Our Roma Office | " | 20.000,20 | | |
| id. | id. | " | 10.000,20 | | |
| Safe Dep. Bk. | id. | " | 1.018,— | | 560 |
| Nat. Bk—Scotdale | id. | " | 335,40 | | |
| id. | id. | " | 10.000,20 | | |
| Nat. Bk—Scranton | id. | " | 100,— | | |
| Exch. Nat. Bk | id. | " | 40.100,20 | | |
| Nat. Bk—S. Bend | id. | " | 5.500,— | | |
| Title Trust | id. | " | 5.000,— | | |
| Nat. Bank | id. | " | 25.000,— | | |
| ty Trust—Butler | id. | " | 2.500,— | | |
| l Bk of New York | Our Salerno Office | " | 400,— | | |
| id. | id. | " | 200,— | | |
| Nat. Bank Pa. | id. | " | 55,— | | |
| id. Trinidad | Our Sassari Office | " | 14.210,— | | |
| id. id. | id. | " | 24.360,— | | |
| id. Telluride | Our Trento Office | " | 142,— | | |
| id. Trinidad | id. | " | 7.480,— | | |
| id. Gallupi | id. | " | 412,— | | 561 |
| id. Trinidad | id. | " | 12.000,— | | |
| id. Renovo | Our Trieste Office | " | 600,— | | |
| id. Warden | Our Udine Office | " | 2.116,— | | |
| id. Christopher | Our Vicenza Office | " | 100,— | | |
| of Eureka | Our Siracusa Office | " | 191,— | | |
| th Trust Co. | id. | " | 100,— | | |
| t Salt Lake | A. Pegazzano & C.—Massa | " | 202,— | | |
| State Bk | Our Torino Office | " | 100,— | | |
| olds Sav. Bk | id. | " | 199,20 | | |
| of West Town | Our Trapani Office | " | 100,— | | |
| of Wierton—Wierton | Our Roma Office | " | 1.250,— | | |
| id. | id. | " | 1.100,— | | |
| id. | id. | " | 1.100,— | | |
| id. | id. | " | 2.000,— | | |
| id. | Our Trieste Office | " | 10.000,— | | |
| id. | Credito Fiumano—Fiume | " | 2.000,— | | |
| | TOTAL | Lit | 1.526.148,48 | | |

**Claimant's Exhibit 198.**

ACHOD & KUHNE Loro Conto Ordinario colla BANCA COMMERCIALE ITALIANA — Sede di Genova
New York chiuso al 10 Settembre 1923

| Pagamento al nostro domicilio. | | | | | | AVERE | | |
|---|---|---|---|---|---|---|---|---|
| Importo | Valuta | 1923 | | Causale | | Importo | Valuta | |
| 51,738,351.88 | | | | | Riporto..... | 51,825,703.14 | | |
| 1.— | | Guigus | 23 | disp. 8284 annuall | ..... | 158.— | Guizars | 22 |
| 577.30 | | | " | 8450/171 " | ..... | 12,500.— | " | 22 |
| 395.85 | | | " | 8476/906 " | ..... | 60.— | " | 22 |
| 103,800.— | | | 25 | " 8322/548 " | ..... | 450.— | " | 25 |
| Lit. 51,843,126.03 | | | 30 | Interessi come da nota scalare | ..... | 4,254.89 | | |
| Lit. 6.— | | | | | | | | |
| 157.55 | Luizlis | 12 | | | | Lit. 51,843,126.03 | | |
| 65.60 | | 24 | 1923 | | | | | |
| 358.90 | | 27 | Luiglio | 1 Saldo Precedende | | Lit. 103,800.— | Guizirs | 30 |
| | | | Settem | 10 disposiziover annuall. | ..... | 15,260,048.48 | Settem | 10 |
| 7.35 | | | | Interessi come de nota | | | | |
| 1,629,770.— | | | | scalare | ..... | 516.92 | | |
| Lit. 1,630,365.40 | | | | | | Lit. 1,630,365.40 | | |
| | | 1923 | | | | | | |
| | | Settem | 10 | Salo Precedende | | Lit. 1,629,770.— | Settem | 10 |

S. E. & O.

Genova li 10-9-23

562

**Claimant's Exhibit 198.**

Sigg. Knauth, Nachod & Kuhne Loro Conto Ordinario colla Banca Commerciale Italiana — New York — chiuso al 10 Settembre

| 1923 | Dare Causale | | Importo | Valuta | 1923 | Causale | | Importo |
|---|---|---|---|---|---|---|---|---|
| | | Riporto ..... | 51,738,351.88 | | | | | |
| Guigus 18 | spese | ..... | 1.— | | Guigus 23 | disp. 8284 | annuall | ..... |
| 30 | Coumnt Massimo Debito come oto note | ..... | 577.30 | | | " 8450/171 | " | ..... |
| | Spese postail, bolli e diverse | ..... | 395.85 | | | " 8476/906 | " | ..... |
| | Saldo a Nuoro | ..... | 103,800.— | | 25 | " 8322/548 | " | ..... |
| | | | Lit. 51,843,126.03 | | 30 | Interessi come da nota scalare | | ..... |
| 563 1923 | | | | | | | | |
| Luiglio 3 | spese R. d' R. | ..... | Lit. 6.— | | | | | |
| 12 | spese telegrafi | ..... | 157.55 | Luizlis 12 | | | | |
| 25 | " | ..... | 65.60 | 24 | 1923 | | | |
| 27 | " | ..... | 358.90 | 27 | Luiglio | 1 Saldo Precedende | | |
| Settem 10 | Spese postail, bolli e diverse | ..... | 7.35 | | Settem | 10 disposiziover annuall. | | ..... |
| | Saldo a Nuoro | ..... | 1,629,770.— | | | Interessi come de nota scalare | | ..... |
| | | | Lit. 1,630,365.40 | | | | | |
| | | | | | 1923 | | | |
| | | | | | Settem | 10 Salo Precedende | | |

S. E. & O.

Genova li 10-9-23

564

# Trustee's Exhibit 1.

## BANCA COMMERCIALE ITALIANA, GENOA LIRES

Form L 16 B—1000—2,23.

| Date | Particulars | Debit: Value Date | Debit: Posted From | Debit: Foreign Amount | Debit: Dollars | Credit: Dollars | Credit: Foreign Amount | Credit: Posted From | Credit: Value Date | | Pur |
|---|---|---|---|---|---|---|---|---|---|---|---|
| 1923 | Brought Forward | | | 42,460,125.97 | 31,500.69 | 37,710.44 | 43,348,750.47 | | | | |
| May 11 | Bot B. C. I. city | 5/14 | 5/14/23 | 150,000. | 7,166.25 | 6,541.31 | 137,000.20 | 8460 | 5/21/23 | Dft | 27,000.20 |
| | To book dif. due on our purch. L. 150,000 on 5/9/23 | | 7098 | — | 18.75 | | | | | | 110,000. |
| 14 | Bot Guaranty Trust Co. | 5/16 | 5/16/23 | 250,000. | 12,256.25 | | | | | | 57,220. |
| | " Philad Natl Bk Pa. | 5/15 | 5/15/23 | 250,000. | 12,162.50 | 5,179.52 | 107,220. | " | " | " | 50,000. |
| | Coll. Themselves | | 5/25/23 | 400,000. | 19,360. | 4,812.50 | 100,000. | 14317 | 5/14/23 | Sold | American Sta |
| 15 | Bot Empire Trust Co city | 5/18 | 5/18/23 | 650,000. | 31,606.25 | 4,812.50 | 100,000. | 14316 | " | " | " |
| | | | | | | 1,972.10 | 41,000. | 8461 | 5/24/23 | Dft | |
| | " Banca di Roma city | 5/16 | 5/16/23 | 250,000. | 12,237.50 | 2,859. | 60,000. | 14303 | 5/14/23 | Sold | D. M. Giuli & |
| | " " " " | 5/16 | " | 400,000. | 19,590. | | 43,893,970.67 | | | | |
| | | | | 44,810,125.97 | | 799.11 | 16,456.85 | 8462 | 5/24/23 | Dft | |
| 18 | Canc. dft 34308 — 8284 | | " | 50056 | 158. | 7.62 | 7,620.41 | 157,583.92 | " | " | " |
| | | | | 44,810,283.97 | | | 1,466.06 | 29,972.60 | " | " | To adj. dif on our |
| 21 | Bot East River Natl Bk city | 5/23 | 5/23/23 | B1046 | 250,000. | 12,143.75 | 108.75 | — | 7221 | | " |
| | " Bca Nat. del Reduce city | 5/22 | 5/22/23 | B1035 | 250,000. | 12,143.75 | 1,278.39 | 26,050. | 8463 | 5/26/23 | |
| | " Equitable Trust Co. city | 5/23 | 5/23/23 | B1045 | 250,000. | 12,143.75 | 23,290.92 | 478,795.40 | " | " | Dft |
| 22 | " Banca di Roma | 5/25 | 5/25/23 | B1064 | 250,000. | 12,056.25 | 4,900. | 100,000. | 14409 | 5/17/23 | Dft |
| | Canc dft 36923 — 8468 | | 6/ 9/23 | 50072 | 1,015. | 50. | 4,875. | 100,000. | 14419 | " | " |
| | | | | 45,811,298.97 | 194,443.31 | 4,840. | 100,000. | 14476 | 5/18/23 | Sold | Pittsburgh Sta |
| | | | | | | 133,066.01 | | | | " | Mellon Natl B |
| | | | | | | 147.60 | 3,000. | 14466 | 5/17/23 | " | Bd Bridge Bk. |
| | | | | | | 97.60 | 2,000. | 14459 | " | | |
| | | | | | | 1,321.43 | 27,118. | 8464 | | " | First Natl Ban |
| | | | | | | | | | | " | " " " |
| | | | | | | 3,984.87 | 81,637.40 | " | 5/29/23 | Dft | 2,118 |
| | | | | | | | 45,016,584.84 | | | | 25,000 |
| | | | | | | 97.40 | 2,000. | 14511 | 5/18/23 | " | |
| | | | | | | 97.40 | 2,000 | 14499 | " | | |
| | | | | | | 7,827.47 | 161,221.20 | 8465 | | Sold | R. K. Babcock |
| | | | | | | 3,654.64 | 75,000.40 | " | 5/29/23 | " | Tampico Bkg. |
| | | | | | | 6,401.34 | 131,791. | 6 | 5/29/23 | Dft | 111,221.20 |
| | | | | | | 9,136.17 | 187,950.10 | " | " | " | |
| | | | | | | 17.01 | 350. | 14550 | 5/19/23 | " | |
| | | | | | | 121.63 | 2,500. | 14544 | " | " | |
| | | | | | | 1,231.55 | 25,300. | 8467 | 6/ 1/23 | Sold | Morelli State B |
| | | | | | | 1,239.05 | 24,439. | 14595 | 5/21/23 | " | Melchieri Bros |
| | | | | | | | 45,629,136.54 | | | Dft. | |
| | | | | | | 2,422.44 | 49,745. | 8468 | 5/31/23 | Sold | Harry Geist & |
| | | | | | | 15,799.87 | 325,000.40 | " | " | | |
| | | | | | | 5,673.75 | 116,680.40 | " | " | Dft. | |
| | | | | | | 488. | 10,000. | 14534 | 5/22/23 | " | |
| | | | | | | — | —.20 | 7567 | 5/ 2/23 | " | |
| | | | | | | 2,147.40 | 44,100. | 8469 | 6/ 2/23 | Sold | Bca. N. Giovan |
| | | | | | | 9,585.81 | 197,508.60 | " | " | To adj. dif. on dft | |
| | | | | | | 24,300. | 500,000. | 14651 | 5/23/23 | Dft | |
| | | | | | | 24,150. | 500,000. | 14682 | 5/24/23 | " | |
| | | | | | | | 47,372,171.14 | | | Sold | Bca Popolare |
| | | | | | | 5,228.68 | 107,781. | 8470 | | " | " " |
| | | | | | | | | | | Dft. | 7,781. |
| | | | | | | 17,861.70 | 370,055. | " | 6/ 6/23 | | 100,000. |
| | | | | | | | | | | | 10,000. |
| | | | | | | 276,098.82 | 47,850,007.14 | | | " | 250,000. |

**Trustee's Exhibit 1.**

565

BANCA COMMERCIALE ITALIANA, GENOA LIRES

Sheet No.

| Debit | | | | | | Credit | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Value Date | Posted From | Foreign Amount | Dollars | Dollars | Foreign Amount | Posted From | Value Date | Particulars | | | Date 1923 |
| | | | 42,460,125.97 | 31,500.69 | 37,710.44 | 43,348,750.47 | | | | | | |
| | 5/14 | 5/14/23 | B922 | 150,000. | 7,166.25 | 6,341.31 | 137,000.20 | 8460 | 5/21/23 | Dft 27,000.20 5/21 | | May 11 |
| 150,000 on | 5/9/23 | | 7095 | — | 18.75 | | | | | 110,000. " | | |
| | 5/16 | 5/16/23 | B968 | 250,000. | 12,256.25 | | | | | 57,220. 5/21 | | |
| | 5/15 | 5/15/23 | B966 | 250,000. | 12,162.50 | 5,179.52 | 107,220. | " | " | " 50,000. " | | |
| | | 5/25/23 | 8326 | 400,000. | 19,360. | 4,812.50 | 100,000. | 14317 | 5/14/23 | Sold American State Bank Dt. | 5/14 | |
| | 5/18 | 5/18/23 | B981 | 650,000. | 31,606.25 | 4,812.50 | 100,000. | 14316 | " | " " " " " " | 5/14 | |
| | | | | | | 1,972.10 | 41,000. | 8461 | 5/24/23 | Dft | | 12 |
| | 5/16 | 5/16/23 | B974 | 250,000. | 12,237.50 | 2,859. | 60,000. | 14303 | 5/14/23 | Sold D. M. Giuli & Son, Milwaukee B. C. I. | | |
| | 5/16 | " | B973 | 400,000. | 19,590. | | 43,895,970.67 | | | | | |
| | | | | 44,810,125.97 | | 799.11 | 16,456.85 | 8462 | 5/24/23 | Dft | | 14 |
| | | " | 50056 | 158. | 7.62 | 7,620.41 | 157,583.92 | " | " | " | | |
| | | | | 44,810,283.97 | | 1,466.06 | 29,972.60 | " | " | To adj. dif on our sale Lit. 300,000 to Pollock | | |
| | 5/23 | 5/23/23 | B1046 | 250,000. | 12,143.75 | 108.75 | — | 7221 | | " | | |
| | 5/22 | 5/22/23 | B1035 | 250,000. | 12,143.75 | 1,278.39 | 26,050. | 8463 | 5/26/23 | | | 566 |
| | 5/23 | 5/23/23 | B1045 | 250,000. | 12,143.75 | 23,290.92 | 478,795.40 | " | " | Dft | | |
| | 5/25 | 5/25/23 | B1064 | 250,000. | 12,056.25 | 4,900. | 100,000. | 14409 | 5/17/23 | Dft | | 15 |
| | | 6/ 9/23 | 30072 | 1,015. | 50. | 4,875. | 100,000. | 14419 | " | " | | |
| | | | | 43,811,298.97 | 194,447.31 | 4,840. | 100,000. | 14476 | 5/18/23 | Sold Pittsburgh State Bank Pg. B. C. I. | 5/17 | |
| | | | | | | 133,066.01 | | | | " Mellon Natl Bank Pg. " | 5/17 | |
| | | | | | | 147.60 | 3,000. | 14466 | 5/17/23 | " Bd Bridge Bk. Chicago B. C. I. | 5/18 | 16 |
| | | | | | | 97.60 | 2,000. | 14459 | " | | | |
| | | | | | | 1,321.43 | 27,118. | 8464 | | " First Natl Bank H. Fels R. Poutaguali | | |
| | | | | | | | | | | " " " " Hagleton C. Petronio | | |
| | | | | | | 3,984.87 | 81,637.40 | " | 5/29/23 | Dft 2,118 5/29 | | |
| | | | | | | | 45,016,584.84 | | | 25,000 5/25 | | |
| | | | | | | 97.40 | 2,000. | 14511 | 5/18/23 | " | | |
| | | | | | | 97.40 | 2,000 | 14499 | " | | | |
| | | | | | | 7,827.47 | 161,221.20 | 8465 | | Sold R. K. Babcock & Co. city M. La Guaragua | | 17 |
| | | | | | | 3,654.64 | 75,000.40 | " | 5/29/23 | " Tampico Bkg. Co. M. A. Valedante | | |
| | | | | | | 6,401.34 | 131,791. | 6 | 5/29/23 | Dft 111,221.20 5/29 | | |
| | | | | | | 9,136.17 | 187,950.10 | " | " | " | | |
| | | | | | | 17.01 | 350. | 14550 | 5/19/23 | " | | 18 |
| | | | | | | 121.63 | 2,500. | 14544 | " | " | | |
| | | | | | | 1,231.55 | 25,300. | 8467 | 6/ 1/23 | Sold Morelli State Bank Seu. T. Elia | | |
| | | | | | | 1,239.05 | 24,439. | 14595 | 5/21/23 | " Melchieri Bros. Pa.—E. Tartaglini | | |
| | | | | | | | 45,629,136.54 | | | Dft. | | 19 |
| | | | | | | 2,422.44 | 49,745. | 8468 | 5/31/23 | Sold Harry Geist & Co. city—O. Tacetti | | |
| | | | | | | 15,799.87 | 325,000.40 | " | " | | | |
| | | | | | | 5,673.75 | 116,680.40 | " | " | Dft. | | 21 |
| | | | | | | 488. | 10,000. | 14534 | 5/22/23 | " | | |
| | | | | | | — | —.20 | 7567 | 5/ 2/23 | " | | |
| | | | | | | 2,147.40 | 44,100. | 8469 | 6/ 2/23 | Sold Bca. N. Giovannangeli Dt. D. Anderson | | |
| | | | | | | 9,585.81 | 197,508.60 | " | " | To adj. dif. on dft 530,435—8403 | | |
| | | | | | | 24,300. | 500,000. | 14651 | 5/23/23 | Dft | | 22 |
| | | | | | | 24,150. | 500,000. | 14682 | 5/24/23 | " | | |
| | | | | | | | 47,372,171.14 | | | Sold Bca Popolare Fugazitfr—BCI | 5/23 | |
| | | | | | | 5,228.68 | 107,781. | 8470 | | " " " " " | 5/24 | |
| | | | | | | | | | | Dft. 7,781. 6/6 | | |
| | | | | | | 17,861.70 | 370,055. | " | 6/ 6/23 | 100,000. | | |
| | | | | | | | | | | 10,000. 6/6 | | |
| | | | | | | 276,094.82 | 47,850,007.14 | | | " 250,000. 110,055.—6/6 | | |

567

568

**Trustee's Exhibit 2.**

| Rate | Dollar Amount |
|---|---|
| | 3 354 90 |
| | 267 85 |
| | 51 45 |
| | 4 025 54 |
| | 1 886 07 |
| | 9 585 81 |

Advised by:
Checked by: B. H.
Approved:

569

| Rate | Dollar Amount |
|---|---|
| 48675 | 730 13 |
| 488 | 212 27 |
| | 942 40 |
| 4825 | 2 412 50 |
| 483¾ | 3 354 90 |

Advised by:
Checked by: B. H.
Approved:

| Rate | Dollar Amount |
|---|---|
| 487 | 267 85 |

570

Advised by:
Checked by: B. H.
Approved:

| Rate | Dollar Amount |
|---|---|
| 490 | 2 45 |
| 490 | 49 00 |
| 490 | 51 45 |

Advised by:
Checked by: B. H.
Approved:



*Trustee's Exhibit 2.* 571

| Rate | Dollar Amount |
|---|---|
| 489 | 694 87 |
| " | 1 191 20 |
| 489 | 1 886 07 |

Advised by:
Checked by: B. H.
Approved:

| Rate | Dollar Amount |
|---|---|
| 4875 | 29 74 |
| 484 | 449 16 |
| | 478 90 |
| 488 | 763 73 |
| 484 | 2 782 91 |
| 484⅝ | 4 025 54 |

572

Advised by:
Checked by: B. H.
Approved:

573

**Trustee's Exhibit 3.**

Founded 1852
K N & K
New York.

**Refund Department.**

KNAUTH, NACHOD & KUHNE
120 Broadway

..... New York, .....
.....
.....

GENTLEMEN:

We desire to have payment stopped on the following drafts. Kindly, therefore, cancel our advice of same and notify us promptly that you have done so.

| Number | Amount | Drawn on | Drawn by | When Advised |
|---|---|---|---|---|

192

**Trustee's Exhibit No. 4.**

KNAUTH, NACHOD & KUHNE
New York

Cancellation of Drafts to ..... No.....
.....

We beg to inform you of the cancellation of the following Drafts, which are in our possession

| Originally Advised Date | S. S. No. | Number | Drawn By | City | Drawn on | Currency | Amount |
|---|---|---|---|---|---|---|---|

Sigg. KNAUTH, NACH

| 1923 | Causale | DARE |
|---|---|---|
| Maggio 21 | N Y. 89517 | |
| " | 92581 | |
| " | —3 | |
| " | —630 | |
| " | | spere |
| " | pag Tauetto f | |
| " | comenle " | |
| 22 | disp. list 8458 | |
| " | | " |
| " | | " |
| " | " " 8459 | |
| " | " " —8 | |
| " | " " —7 | |
| " | | " |
| " | " " 8460 | |
| " | | " |
| " | All-o. fae. dolenico | |
| " | conveny e " | |
| " | disp. list 8459 | |
| " | —60 | |
| " | —" | |
| " | —57 | |
| " | | " |
| " | | " Telig |
| 23 | boni fico Banca Pep. | fugay |

Riporto Li

A riportare Lit

**Trustee's Exhibit 5.**

577

Rec'd Uun 11, 1923
Ans'd

Sigg. KNAUTH, NACHOD & KUHNE Loro Conto ordinario colla BANCA COMMERCIALE ITALIANA — Sede di Genova
New York al 25 Maggio—1923

| | Pagamento al nostro domicilio. | | | | AVERE | |
|---|---|---|---|---|---|---|
| | Importo | Valuta | 1923 | Causale | Importo | Valuta |
| Riporto Lit. | 43,460,620.31 | | | | | |
| ..... | 10,000.— | Maggio | 21 | | | |
| ..... | 50,000.— | | 21 | | | |
| ..... | 60,000.— | | 21 | | | |
| ..... | 50,000.— | | 21 | | | |
| ..... | 1.— | | " | | | |
| ..... | 24,439. | | 21 | | | |
| ..... | 62.30 | | " | | | |
| ..... | 118,525.15 | | 21 | | | |
| ..... | 30.10 | | " | | | 578 |
| ..... | 1.— | | " | | | |
| ..... | 29,400.20 | | 21 | | | |
| ..... | 63,864.50 | | 21 | | | |
| ..... | 60,400.— | | 21 | | | |
| ..... | 11.30 | | " | | | |
| ..... | 11,979.25 | | 21 | | | |
| ..... | 4.70 | | " | | | |
| ..... | 10,000.— | | 22 | | | |
| ..... | 33.— | | " | | | |
| ..... | 104,627.40 | | 21 | | | |
| ..... | 57,220.— | | 21 | | | |
| ..... | 27,000.20 | | 21 | | | |
| ..... | 14,997.45 | | 21 | | | |
| ..... | 45.70 | | " | | | |
| ..... | 24.90 | | " | | | |
| ..... | 500,000.— | | 23 | | | 579 |
| A riportare Lit. | 44,653,287.46 | | | | | |

S. E. & O.
Genova li 26-5-23

*Trustee's Exhibit #5—Cont'd.*

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Riporto Lit. | 44,653,287.46 | | | | Riporto Lit. | 44,208,449.59 | |
| ..... | .30 | " | Maggio 23 | versf. merirt laveg of East River | ..... | 250,000.— | Maggio 23 |
| ..... | 1.— | " | " | opo el. Milano—liquidat. librette | ..... | 19,639.75 | 22 |
| ..... | .30 | " | " | "Credito of Equi trust | ..... | 250,000.— | 23 |
| ..... | 500,000.— | Maggio 24 | Maggio 24 | verf. creditor p.u.c. | ..... | 750,000.— | Maggio 24 |
| ..... | .30 | " | 25 | " Banca Roma of ofsede Trini | ..... | 250,000.— | 25 |
| ..... | 41,000.— | 24 | " | of uineng | ..... | 400,000.— | 25 |
| ..... | 16,456.85 | 24 | | | | | |
| ..... | 157,583.92 | 24 | | | | | |
| ..... | 29,972.60 | 24 | | | | | |
| ..... | 24.60 | 24 | | | | | |
| ..... | 1.— | " | | | | | |
| ..... | 25,000.— | 25 | | | | | |
| ..... | 3,000.— | 25 | | | | | |
| ..... | 4.30 | " | | | | | |
| ..... | 2,065.— | 25 | | | | | |
| ..... | 9.20 | " | | | | | |
| ..... | 200.— | 25 | | | | | |
| ..... | 8.80 | " | | | | | |
| ..... | 5.55 | " | | | | | |
| ..... | .30 | " | | | | | |
| ..... | 1.— | " | | | | | |
| ..... | .20 | " | | | | | |
| ..... | 26,050.— | 26 | | | | | |
| ..... | 478,795.40 | 26 | | | | | |
| ..... | 4.70 | " | | | | | |
| ortare Lit. | 45,933,472.78 | | | | Lit. | 46,128,089.34 | |
| ..... | 194,616.56 | | | | | | |
| Lit. | 46,128,089.34 | | Maggio 26 | Saldo Precedente | Lit. | 194,616.56 | Diverse |

580 *Trustee's Exhibit #5—Cont'd.*

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| | | | Riporto Lit. | 44,653,287.46 | | | |
| Maggio 23 | | Spere | ..... | .30 | " | Maggio 23 | versf. merirt laveg of East River |
| " | | " | ..... | 1.— | " | " | opo el. Milano—liquidat. librette |
| " | | " | ..... | .30 | " | " | "Credito of Equi trust |
| 24 | Conifico fugazi | | ..... | 500,000.— | Maggio 24 | Maggio 24 | verf. creditor p.u.c. |
| " | | " | ..... | .30 | " | 25 | " Banca Roma of ofsede Trini |
| 25 | disp. list 8461 B. | | ..... | 41,000.— | 24 | " | of uineng |
| " " | " 8462 A. | | ..... | 16,456.85 | 24 | | |
| " " | " 8462 B. | | ..... | 157,583.92 | 24 | | |
| " " | " 8462 C. | | ..... | 29,972.60 | 24 | | |
| " | | " | ..... | 24.60 | 24 | | |
| " | | " | ..... | 1.— | " | | |
| " " | " 8464 A. | | ..... | 25,000.— | 25 | | |
| 581 " | pag T. Cianitinotto-Catania | | ..... | 3,000.— | 25 | | |
| " | conveny e spere | | ..... | 4.30 | " | | |
| " | "P. Barbera—Lpoleto | | ..... | 2,065.— | 25 | | |
| " | conveny e | " | ..... | 9.20 | " | | |
| | Zelwig Deleoute-Fireys | | | | | | |
| " | convey e | " | ..... | 200.— | 25 | | |
| " | | " | ..... | 8.80 | " | | |
| " | | " Telig | ..... | 5.55 | " | | |
| " | | " | ..... | .30 | " | | |
| " | | " | ..... | 1.— | " | | |
| " | | " | ..... | .20 | " | | |
| 25 | disp. List 8463 A. | | ..... | 26,050.— | 26 | | |
| " " | " —B. | | ..... | 478,795.40 | 26 | | |
| " | | " | ..... | 4.70 | " | | |
| | | | A riportare Lit. | 45,933,472.78 | | | |
| 582 Maggio 26 | Saleto Creditore | | ..... | 194,616.56 | | | |
| | | | Lit. | 46,128,089.34 | | Maggio 26 | Saldo Precedente |

583

**Trustee's Exhibit 6.**

Rec'd Sep 25 1923
Ans'd

Segreteria B.

Genoa, September 7th, 1923.

MIDDLETON S. BORLAND, ESQ.,
Receiver for Messrs Knauth, Nachod & Kuhne,
NEW YORK.

DEAR SIR:

We are in receipt of your favour of the 24th. ult. and with regard to the first item you mention, 584
viz:
April 2nd. Lit. 2000,00.—Money Order 8426—
we have to inform you that we have no reference whatever to any such number, but presume that the item in question must be one of two orders passed to us by cable on April 2nd., viz:

1) Lit. 2000.—to Luigi Brandonisio fu Giuseppe of Carbonara, Bari, the payees receipt for which was duly mailed to Messrs. K. N. & K. on May 7th, 1923.
2) Lit. 2000.—to Filohena Trotta, Palazzo Pinto, Aversa, Caserta, the payees receipt for which was duly mailed to Messrs. K. N. & K. on April 19th, 1923. 585

As to the second item cited in your letter, viz: April 24th, 1923 Lit. 50.000.—Collection No. 8132— we regret to have to inform you that we find no trace of ever having received the transaction for execution.

Regarding the drafts you mention, viz:

586 *Trustee's Exhibit 6.*
*Trustee's Exhibit 7.*

| | | | | | |
|---|---|---|---|---|---|
| May 18, 1923 | Lit. | 158,00 | Cancelled Draft | | 34308/8284 |
| May 29, 1923 | " | 450,00 | " | " | 419548/8322 |
| June 6, 1923 | " | 2500,00 | " | " | 89135/8450 |
| June 6, 1923 | " | 10000,00 | " | " | 89171/8450 |
| June 8, 1923 | " | 60,00 | " | " | 733906/8476 |

we would refer you to our letter of June 25th, in which we credited you with the second draft listed above (Lit. 450.—) while the other four were passed to your credit in our letter of June 22nd. last.

We are, Dear Sir,

587 Yours very truly,
BANCA COMMERCIALE ITALIANA.
Sede di Genova.

**Trustee's Exhibit 7.**

August 24, 1923.
F. X. ACCTG.

BANCA COMMERCIALE ITALIANA,
Genoa, Italy.
Gentlemen,

I have examined your statements of the account of Knauth, Nachod & Kuhne as of June 15th, 1923, showing a balance in their favor of Lit.
588 87,351.26 and now wish to draw your attention to the following discrepancies:

WE CREDIT—YOU DO NOT DEBIT:

April 2, 1923 Lit. 2,000.00 Money order No. 8426 I surmise that this Money Order has not been effected. Will you kindly inform us as to the actual status of said order in order to enable me to make the necessary adjustments on my books.

*Trustee's Exhibit 7.* 589

WE DEBIT—YOU DO NOT CREDIT:

| | | | | |
|---|---|---|---|---|
| April 24, 1923 | Lit. 50,000.00 | Collection | | #8132. Will you please inform me when you expect to collect this item and place the proceeds to my credit. |
| May 18, 1923 | Lit. 158.00 | Cancelled | Draft | #84308/8284 |
| May 29, 1923 | Lit. 450.00 | " | " | #419546/8322 |
| June 6, 1923 | Lit. 2,500.00 | " | " | #89135/8450 |
| June 6, 1923 | Lit. 10,000.00 | " | " | #89171/8450 |
| June 8, 1923 | Lit. 60.00 | " | " | #733906/8476 |

590

I am awaiting your letter confirming that you have taken note of the cancellation of the aforementioned drafts and that you have credited my account with the above amounts.

Kindly investigate the differences referred to above and advise me of the results at an early date.

Very truly yours,

MIDDLETON S. BORLAND,
Receiver.

591

598 *Report and Opinion of Special Master.*

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

| | |
|---|---|
| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL, MARY W. KNAUTH and THEODORE W. KNAUTH, doing<br>599 business as co-partners under the firm name and style of KNAUTH, NACHOD & KUHNE, and OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL and THEODORE W. KNAUTH, individually,<br>Bankrupts,<br>and<br>MARY W. KNAUTH,<br>Alleged Bankrupt. | In Bankruptcy No. 34986 Report No. 27 of the Special Master |

600

Reclamation of

FIRST NATIONAL BANK OF TRINIDAD, COLO.

The petition of the First National Bank of Trinidad, Colorado, contains two causes of action. In the first cause of action it alleges the filing of an involuntary petition in bankruptcy against Knauth, Nachod & Kuhne on or about June 15, 1923, and the appointment of Middleton S. Borland as Receiver, and the subsequent election and

qualification of Middleton S. Borland as Trustee. It then alleges that prior to May 19, 1923, the bankrupts, to induce the petitioner to enter into trade relations with them, offered to accept from the petitioner from time to time sums of money, and use the same for the payment of drafts to be drawn by the petitioner on certain designated foreign correspondents of the bankrupts; that about May 19, 1923, the petitioner, in acceptance of said offer, drew its draft No. 61,161 on Banca Commerciale Italiana at Sassari, Italy, whereby it directed the said Italian Bank to pay to Zara Sanna Giovanni on presentment of said draft, the 602
sum of 24,360 lire; and that on or about the same day the petitioner delivered to the bankrupts the sum of $1,191.20 to be used for the payment of said draft on presentment, and not otherwise; that the bankrupts agreed with the petitioner to use same for the payment of said draft, and for no other purpose; that the bankrupts failed to cause said sum of $1,191.20 or any part of it to be used for the payment of said draft, and that the said sum has come into and is now in the possession and control of the Trustee.

The second cause of action alleges in addition to the above facts that there existed to the knowledge of the bankrupts a custom, 603
on the part of the bankrupts the Banca Commerciale Italiana to charge the account of the bankrupts with the amount of drafts drawn against it on the receipt of advice thereof from the bankrupts, and thereupon to set aside and appropriate said amount for the payment of said drafts when presented; that on or about May 22, 1923, the bankrupts notified the Banca Commerciale Italiana of the drawing of the said draft,

and requested the Banca Commerciale Italiana to charge the same to their account; that upon receipt of said advice, the Banca Commerciale Italiana, on or about June 4, 1923, with the knowledge and acquiescence of the bankrupts, set aside in a separate fund, and appropriated for the payment of said draft the sum of 24,360 lire, and charged the same to the bankrupts; that the Receiver, before the presentation or payment of said draft, instructed the Banca Commerciale Italiana not to pay it, and to return to him the amount so set apart and appropriated. Pursuant to said direc-
605 tion of the Receiver, the Banca Commerciale Italiana returned to him the moneys so set apart, and the same are now in the Trustee's possession; that the draft was duly presented and dishonored, and due notice thereof given to the Trustee.

The petitioner prays that it be adjudged to be entitled to, and have a lien upon the moneys in the hands of the Trustee in the amount of $1,191.20, with interest thereon from May 19, 1923, superior to all rights of the bankrupts of the Trustee or any creditor; and that the Trustee be decreed to pay said sum with interest to the petitioner out of the moneys in his hands.

606 The Trustee denies all the allegations in the petition except the filing of the petition and the appointment of a Receiver.

O'Brien, Boardman, Parker & Fox, Esqs.—For the Petitioner.

Rosenberg & Ball, Esqs.—for the Trustee.

Stephenson, Special Master: The bankrupt firm of Knauth, Nachod & Kuhne were dealers in foreign exchange, and sought the business of inland

banks who did not have connections with foreign banks. They sent to inland banks, including the petitioner in this case, a document entitled "List of Foreign Correspondents." This document referred to the world wide facilities for carrying on a foreign exchange business possessed by Knauth, Nachod & Kuhne, and contained a list of their foreign correspondents. These were banks located in cities throughout the world.

This document described three methods of effecting payment in foreign countries through the service offered by Knauth, Nachod & Kuhne.— (1) "K. N. & K. Drawing Service"; (2) "K. N. 608
& K. Money Order Service"; (3) "K. N. & K. Cable Transfers."

The facts in this case relate to the use of K. N. & K. Drawing Service. The terms and conditions of this service and the acceptance thereof by the petitioner constitute the contract in this case. Knauth, Nachod & Kuhne furnished the petitioner with blank draft forms bound in a book, together with appropriate blanks for advising Knauth, Nachod & Kuhne. The draft forms bore only the name of the petitioner. They were in the usual draft form with blanks for the use of the payee, the amount, the name of the drawee bank, and for 609
the signature of the petitioner. Upon receipt by Knauth, Nachod & Kuhne from the petitioner of an advice of draft, accompanied with adequate funds payable at par in New York at the rate quoted, Knauth, Nachod & Kuhne agreed to forward their advice of the same, and to "provide the drawee bank with funds sufficient for the payment of the draft abroad, by a transfer of credit from our balance, or otherwise, provided the draft is drawn on a bank named in our latest list of

610 *Report and Opinion of Special Master.*

correspondents." Lost drafts would be replaced, after the cancellation of the original draft had been effected, abroad, and re-transfer of credit received by Knauth, Nachod & Kuhne, upon furnishing a bond of indemnity. Knauth, Nachod & Kuhne agreed to redeem unpaid drafts at the buying rate prevailing at the time they were presented for redemption, and not in the amount paid for the original draft. In case the funds received by Knauth, Nachod & Kuhne with the advice should be less than the quoted rate, Knauth, Nachod & Kuhne had the right either to hold the
611 same and advise the petitioner of the deficit or to advise the draft abroad and require the petitioner to remit the deficit. If the funds received were more than the quoted rate, Knauth, Nachod & Kuhne could either advise the petitioner of the excess or advise the draft abroad and return the excess to the petitioner.

The document, after describing what Knauth, Nachod & Kuhne agrees to do, states as follows:

> "Under this arrangement, our correspondents in this country act as PRINCIPALS, and issue drafts in their own names, our name not appearing thereon. In other
612 words, we are employed merely as the agents of the drawers for the purpose of advising the issue of their drafts and providing the drawee banks with sufficient funds to cover their payment."

On May 19, 1923, the bankrupts notified the petitioner that the rate for 24,360 Italian lire on that day would be .0489 per lire. Thereupon the petitioner drew its draft No. 61,161 for 24,360 lire, payable to Zara Sanna Giovanni or order, on

the Banca Commerciale Italiana, Sassari, Italy, using one of the blanks, furnished it by Knauth, Nachod & Kuhne. The petitioner sent Knauth, Nachod & Kuhne an "advice," which stated that pursuant to the terms and conditions covering Knauth, Nachod & Kuhne's drawing service, the petitioner sold a draft bearing No. 61,161 for 24,360 lire, and requested Knauth, Nachod & Kuhne to protect the same upon presentation. It gave the name of the payee and the name of the bank on which it was drawn, and stated that the sum of $1,191.20 was remitted which was at the rate of .0489 quoted. The petitioner, with this advice, 614
sent to the bankrupts $1,191.20, which was included in the petitioner's check for $3,518.95. The check included moneys sent in connection with other advices of the same character. This advice and the check were received by the bankrupts on May 22, 1923, and receipt thereof acknowledged. The check was deposited by the bankrupts in their general checking account in the Guaranty Trust Company on May 22, 1923, and the bankrupts received credit therefor on that day. Thereafter on May 22, 1923, the bankrupts mailed to the Banca Commerciale Italiana at its general office six papers known as the "Steamer Block," and a duplicate thereof was mailed to the Sassari 615
branch of the Banca Commerciale Italiana. This "Steamer Block" contained a list of drafts issued by inland banks, and by the bankrupts themselves, giving the number of each draft, the name of the drawer, the address of the drawer, the date, the name of the person in favor of whom the draft was drawn, and the amount of the draft in lire, and requested the Banca Commerciale Italiana to "honor the above listed drafts, charging the same to our account." Among the drafts

listed was the one above referred to, No. 61,161, drawn by the First National Bank of Trinidad, Colorado, in favor of Zara Sanna Giovanni for 24,360 lire.

The bankrupts carried an account in lire with the Banca Commerciale Italiana, and the relation between the bankrupts and the Italian bank was that of depositor and banker. The bankrupts credited the Italian Bank with the drafts drawn by them on that bank, with all advices to pay drafts issued by other parties, including the petitioner in this case, with cable transfers sold,
617 and with any other direction to pay given the Italian Bank. The bankrupts charged the Italian bank with cable transfers purchased for their account in this bank, and with any other form of remittance or transfer made for their account to the Italian bank. These debit and credit entries were made in the bankrupt's books at the time of the issuance of the draft or of the advice to pay, and the case of advices and drafts sent by mail, the credit given by the bankrupts to the Italian bank would occur before the arrival of the advice or draft, and before the corresponding charge would be made by the Italian bank. At certain times also, the bankrupts had the right,
618 by agreement with the Italian bank, to overdraw or over-advise their account within limited amounts.

The aforesaid "Steamer Block" was received by the Banca Commerciale Italiana on or before June 4, 1923, and the account of Knauth, Nachod & Kuhne was debited with the aggregate amount of the drafts referred to in the Steamer Block, and simultaneously on its books, an account termed "Drafts Payable" was credited with such amount. In this account were also credited

amounts of drafts advised to the Banca Commerciale Italiana for payment by other depositors or clients of the Banca Commerciale Italiana, in addition to the bankrupts. This practice was recognized as proper by the bankrupts. Interest was allowed to the bankrupts on the amount of the balance standing to their general credit. No interest was allowed by the Banca Commerciale Italiana on the account termed "Drafts Payable" and the only compensation received by the Banca Commerciale Italiana for their service in honoring drafts was the use of the funds standing to the credit of the account termed "Drafts Payable." 620

It is the practice in international banking transactions for the drawee bank, upon receipt of advice that a draft had been drawn against it, immediately to charge the current account of its client with the amount advised, and to credit another account known as "Unpresented Drafts Drawn" or some similar designation, and it is also the practice in foreign banking transactions, upon receipt by the drawee bank of directions to cancel any advice theretofore given, immediately to cancel the same, and recredit the client in its account current, without the client's assigning any reason for such cancellation. This procedure began at a time when banks did not have the facilities of suddenly raising cash; and, when they were notified by a client of what they would have to meet, they immediately put themselves in possession of sufficient cash to meet their obligations. Originally they held this money apart, practically earmarked to meet the advised obligations, and no interest was paid on same. With the change in banking facilities, which enabled banks, by 621

means of rediscounts and call loans, to raise cash on short notice, the practice of setting aside funds was discontinued, but the practice of not paying interest on the amount of advised drafts was continued. Such practice was followed by Knauth Nachod & Kuhne in its dealings with Banca Commerciale Italiana, but cancellation advices were not given by Knauth, Nachod & Kuhne to the Banca Commerciale Italiana in the case of drafts issued by inland banks, except upon request by the inland bank so to do.

623 After the Receiver was appointed, he had communications with the Banca Commerciale Italiana, and pursuant to his direction, the Italian bank recredited all amounts standing in their drafts payable account which had not been paid, and remitted the amount thereof to the Receiver. The draft in question in this case was presented to the Banca Commerciale Italiana and dishonored. It was then returned to the purchaser thereof, Bachesio Tabasco, and thereupon the petitioner paid to Bachesio Tabasco the sum of $1,128.87. Bachesio Tabasco delivered the said draft to the petitioner.

624 It was known to Knauth, Nachod & Kuhne that between the time of the sending of a steamer block or draft and the time it would be presented, a certain interval of time would elapse, and based upon such estimation, they would provide funds usually by cable transfer to meet the drafts at the time of presentation.

Under its first cause of action, the petitioner seeks to recover the amount paid by it to the bankrupts, and offers to trace this amount into the hands of the Trustee. It claims that as to this amount the bankrupts were Trustees. The

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decision of this question must turn on a determination as to what the agreement was between the petitioner and the bankrupts. To my mind, the contract, reduced to its lowest terms, is simply a promise by the bankrupts in consideration of the money paid to them by the petitioner, to provide the drawee bank with funds to pay the draft upon presentation. The means to be used by the bankrupts to accomplish this purpose are entirely of their own choosing. It is contended that the statement in the terms and conditions of the drawing service that "we are employed merely as the agents of the drawers for the purpose of advising the issue of their drafts and providing the drawee banks with sufficient funds to cover their payment" proves the relation of principal and agent between the petitioner and Knauth, Nachod & Kuhne, and that Knauth, Nachod & Kuhne assumed a fiduciary obligation as to the money received by it from the petitioner. But the relation of principal and agent does not follow the mere use of those words. (*Beecher* vs. *Cosmopolitan Trust Company*, 239 Mass., 48). The existence or non-existence of such relationship must be determined from the whole contract. Clearly, it was not intended that Knauth, Nachod & Kuhne should represent or act for or derive their authority from the petitioner, or that they should be subject to the control and direction of the petitioner. Knauth, Nachod & Kuhne contracted to produce a specified result, namely, to provide the drawee bank with sufficient funds to meet the drafts. In producing this result, they could use their own means and select their own agents free from the control of the petitioner. They were independent contractors. (*Casement* vs. *Brown*

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148 U. S., 615; *Insurance Company* vs. *Shipping Board*, 290 Fed., 182). It certainly was not the intention of the parties that the petitioner assume the risk of loss of the fund received by Knauth, Nachod & Kuhne, or that Knauth, Nachod & Kuhne should keep such fund separate from its own funds, or assume the obligation to account for the same.

It is contended that the petitioner paid this money to Knauth, Nachod & Kuhne for a specific purpose; that it was not a general deposit by which the petitioner became a creditor and
629 Knauth, Nachod & Kuhne a debtor, and that the decisions hold that money deposited with a bank for a specific purpose is held by the bank in trust. In any business transaction, one who pays money to another pays it for a specific purpose. A may give money to B for B's specific promise to build him a house, or A may give money to B for B's promise to pay him back on demand—the usual relation of depositor and banker. Or A may give money to B for B's promise to provide adequate funds to meet A's drafts—that is this case. If A entrusts money to B with the intention that B use that particular money to buy a horse for A,
630 then B becomes A's agent, and the money remains A's. In the first case, A gives the money to B in return for B's promise. In the latter case, B is acting for A, and under his direction, and subject to his control. It is, therefore, immaterial whether B's promise is specific or general. The essential element is what A and B agree as to the ownership of the money paid. In this case, the parties could not have intended the ownership of the money paid by the petitioner to remain in it. It was the bankrupt's consideration for their

promise to provide funds to meet a draft. It is, furthermore, immaterial that Knauth, Nachod & Kuhne did not credit the petitioner with the amount received by them, for they did not agree to return the money; they agreed to provide funds to meet a draft drawn by the petitioner. Instead of a promise by Knauth, Nachod & Kuhne to return the money, the petitioner accepted a promise by Knauth, Nachod & Kuhne to provide funds to meet a draft drawn by it. In neither case is a trust relationship established.

*Beecher* vs. *Commonwealth Trust Company*, supra, decides, under facts which are practically 632
the same as the facts in this case, that there is no trust relationship, and that the sole obligation of the bank is contractual.

*Ligniti* vs. *Mechanics & Metals National Bank*, 230 N. Y., 415, holds that there is no trust relationship where money is paid to a bank for the bank's agreement to provide foreign funds by cable. The principle involved in the *Ligniti* decision applies to this case. In the *Ligniti* case, the bank promised that the foreign bank, upon receipt of cable, would pay the beneficiary named in the cable. In this case the bankrupts promised to have funds at the drawee bank to meet a draft 633
drawn by the petitioner when it should be presented. If there was no trust relationship in the *Ligniti* case, there can be none in this case. The same principle was recognized in *Gravenhorst* vs. *Zimmerman*, 236 N. Y., 22; *Safian* vs. *Irving National Bank*, 202 App. Div., 459, affirmed 256 N. Y., 513; *Taussig* vs. *Carnegie Trust Company*, 156 App. Div., 519; *Kuhne* vs. *Union Trust Company*, 131 Mich., 602; *Samuels* vs. *E. F. Drew & Company*, 296 Fed., 882.

634 *Report and Opinion of Special Master.*

All the above cases represent the more recent decisions of the Courts in the cases dealing with transmission of funds through the use of banking facilities. These decisions take notice of banking practice and the adoption thereof by persons transmitting money to foreign countries. In so far as they are inconsistent with previous decisions, they should control.

The decisions which hold a trust relationship are based upon findings by the courts of an agreement to devote or use the actual money paid the transmitting bank or the actual proceeds of such
635 actual money for the purpose agreed upon.

In re *Jarmulowsky*, 258 Fed. 231, money was to be forwarded to a definite person at a specified place in Europe, and it was understood that the Jarmulowskys were to act as agents only for the sender. This was held trust money, for it appears that the Jarmulowskys were to *forward* the money *only* as agents for the sender. They did not agree to provide funds to meet drafts.

In re *Bologuesi*, 254 Fed. 770, money was given to the bankrupt for investment in a specified manner. The Court held that there was a trust relation. In that case, the bankrupt was to act for the claimant and to purchase drafts and money
636 orders for the claimant and (probably) in his name. The bankrupt there was like a stock broker who accepts money to purchase a specific stock for his customer (*Johnson* vs. *Brooks*, 93 N. Y. 342).

*City of St. Louis* vs. *Johnson*, 5 Dillon 241 and *Cutler* vs. *American Exchange National Bank*, 113 N. Y., 593 were cases where banks accepted money to be remitted to another bank, and the Court held that a trust relationship was estab-

lished. The Court found in those cases, as expressed in *Cutler* vs. *American Exchange National Bank, supra,* that when the same was paid into the remitting bank, "From that moment, the defendant became a depositary of a fund, which was, by its own agreement, devoted to one particular purpose and to no other." Assuming that the agreement was as the Court found, the decision agrees with the principles above mentioned. Whether after the decision in *Ligniti* vs. *Mechanics & Metals National Bank, supra,* the Court would have found that the bank really made such an agreement is doubtful, but in the case at 638
bar, Knauth, Nachod & Kuhne expressly made another agreement. They did not agree to *devote* the funds deposited with them by the petitioner to a particular purpose, but agreed to provide funds to meet a draft when presented at the bank in Italy.

In my opinion, therefore, the petitioner is not entitled to recover under its first cause of action.

Under its second cause of action, the petitioner claims that there was an equitable assignment of so much of the bankrupts' claim against the Banca Commerciale Italiana as was necessary to pay the drafts issued by it. There is no evidence in the dealings between the petitioner and the bank- 639
rupts which shows that either party intended that the petitioner have an equitable assignment or an equitable lien upon any claim the bankrupt may have against the Italian bank. The petitioner had no such intention since the bankrupts did not represent that they had or would have any credit balance against the Italian bank, nor did they agree with the petitioner to establish any such credit balance. The bankrupts had no such intention since they created no credit balance

640 *Report and Opinion of Special Master.*

against the Italian bank specifically to meet the draft drawn by the petitioner. They made such deposits in the Italian bank as were necessary from time to time to meet their obligations. Their method of dealing with the Italian bank was no different from the method of dealing used by an ordinary depositor in his bank. The ordinary depositor maintains such balance as he deems necessary to be available for his needs.

The evidence further shows that the bankrupts at all times, by arrangement with the Italian bank, retained control of all advices sent it, and
641 could cancel such advices at any time. The maintaining of such control shows an intent that there be no assignment. (Re *Interborough Consolidated Corporation*, 288 Fed. 334; *Noyes* vs. *First National Bank*, 180 App. Div. 162, affirmed 224 N. Y. 542).

Equitable liens or equitable assignments should not be created unless necessary to effect the intention of the parties to a contract. Here there is no evidence that the parties contracted or intended that the petitioner have any property right in any right the bankrupts may have against the Italian bank. The bankrupts did not sell to the petitioner or agree to sell any such right.
642 Hence *Fourth Street National Bank* vs. *Yardley*, 165 U. S. 634 does not apply. In the Yardley case, the Court found an intention by the parties that the payee of a draft be secured by an assignment of the drawer's right against the drawee. See *Eastman Kodak Company* vs. *Park National Bank*, 231 Fed. 220, affirmed C. C. A., Second Circuit, 247 Fed. 1002. This case fully discusses the law applicable to equitable assignments, and reviews the cases dealing therewith.

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"In dealing with transactions of this kind, we may go far in giving them any form that will carry out the mutually understood intent. *Sexton* vs. *Kessler*, 225 U. S. 90, 96, 97. But if the intent was doubtful or inconsistent with the legal effect of dominant facts, it must fail. For instance, apart from possible exceptions, a man cannot retain a domicile in one place when he has moved to another and intends to reside there for the rest of his life, by any wish, declaration or intent inconsistent with the dominant facts of where he actually lives and what he actually means to do. *Dickinson* vs. *Brookline*, 181 Massachusetts, 195. In the present case it is agreed that it was expected and understood that no portion of the clearance loan was to be used for any purpose other than to clear securities. But on the other hand, by consent of the bank as it seems, the loan was put into the general deposit account, which was drawn upon for general purposes, at least to the extent of the balance above the loan; the securities released were not kept separate but were used like any others; and no separate account was kept of money received from deliveries of stock so released. What happened as between these parties was simply that all monies received in the course of the day from whatever source went into the firm's deposit account with the bank. So that, even if we take it, as a corollary of what was understood, that the use of the clearance loan was expected to enable the firm

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646 *Report and Opinion of Special Master.*

to repay the loan, it does not appear to have been expected that the proceeds should be appropriated specifically to that end, but simply that the addition of such proceeds to the general funds of the firm would enable the latter to pay within the time allowed."

(*National City Bank* vs. *Hotchkiss*, 231 U. S. 50, at 56).

It is claimed, even admitting that Knauth, Nachod & Kuhne became the owner of the funds
647 paid it by the petitioner, that when they established a credit with the Banca Commerciale Italiana, they held such credit in trust for the benefit of the Petitioner *pro tanto*, and in support of this contention, the petitioner refers to an article by Dean Stone in 21 Columbia Law Review 507. In this article, it is suggested that when the banker has once acquired a credit for transmitting the funds, then any right which the banker thus acquired against the correspondent specifically for the purpose of effecting the transfer may be treated as a *quasi* trust fund held for the benefit of his customer.

648 "In the *Ligniti* case, the banker failed before he had taken any steps to procure the credit pursuant to contractual obligation. Had he actually acquired the credit and specifically appropriated it or a part of it to his undertaking for account of the plaintiff, a very different situation would have arisen and one on which the plaintiff might properly have based a claim that the credit so far as it was an enforceable one

was held by the banker in a fiduciary capacity for the plaintiff."

(21 Columbia Law Review, at 522).

Undoubtedly, as suggested by Dean Stone, the banker could become a Trustee for his customer of his chose in action against the correspondent. But in this case it appears that the parties had no such intention. The bankrupts were under no obligation to create any credit in their favor, and appropriate such credit for the use of the petitioner. Evidently, the petitioner did not intend 650
that it have any property right in any claim by the bankrupt against the Italian bank. In fact, what the petitioner wanted and what it contracted for was that funds should be available in the bank in Italy when the draft was presented, and to accomplish this purpose, it accepted the bankrupts' promise so to do.

The petitioner has not, therefore, established any equitable assignment or lien upon Knauth, Nachod & Kuhne's credit with the Banca Commerciale Italiana.

February 19, 1925.

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**Exceptions to Report of Special Master**

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

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| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL, MARY W. KNAUTH and<br>653 THEODORE W. KNAUTH, doing business as co-partners under the firm name and style of KNAUTH, NACHOD & KUHNE, and OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL and THEODORE W. KNAUTH, individually,<br>Bankrupts,<br>and<br>MARY W. KNAUTH,<br>Alleged Bankrupt. | In Bankruptcy, No. 34,996. |

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NOW comes FIRST NATIONAL BANK OF TRINIDAD, the reclaimant and petitioner herein and hereby excepts to report No. 27 of Hon. Robert P. Stephenson, to whom as Special Master has been referred the reclamation petition of FIRST NATIONAL BANK OF TRINIDAD and the answer thereto, and petitioner excepts to said report on the ground that the Special Master erred in finding—

1. That the bankrupts were dealers in foreign exchange.

2. That the bankrupts acted as independent contractors in their dealings with petitioner, and did not act as agents or fiduciaries of the petitioner.

3. That it was not intended that the bankrupts should represent or act for or derive their authority from the petitioner or that they should be subject to the control and direction of the petitioner or that they should keep the funds separate or assume the obligation to account therefor.

4. That a trust relationship was not established between the bankrupts and the petitioner. 656

5. That the bankrupts did not agree to devote the funds deposited with them by the petitioner to a particular purpose.

6. That the bankrupts did not become trustees of the moneys delivered to them by petitioner under the terms of the drawing service.

7. That at certain times the bankrupts had a right by agreement with the Italian Bank to overdraw or over-advise their account within limited amount.

8. That the only compensation received by the Italian Bank for their services in honoring drafts was the use of the funds standing to the credit of the account termed "drafts payable." 657

9. That it is the practice in foreign banking transactions upon receipt by the drawee bank of directions to cancel any advice theretofore given, immediately to cancel the same and re-credit the client in its current account without the client's assigning any reason for such cancellation.

10. That the contract between the parties was simply a promise by the bankrupts in considera-

658 *Exceptions to Report of Special Master.*

tion of the money paid to them by the petitioner, to provide the drawee bank with funds to pay the draft upon presentation.

11. That it was not the intention of the parties that the ownership of the moneys paid by the petitioner should remain in it but that these moneys were the bankrupts' consideration for their promise to provide funds to meet a draft.

12. That there is no evidence which shows that either party intended that the petitioner have an equitable assignment or an equitable lien upon
659 any claim the bankrupt might have against the Italian Bank.

13. That the bankrupts did not represent that they had or would have any credit balance against the Italian Bank and did not agree to establish any such credit balance.

14. That the bankrupts did not create any credit balance against the Italian Bank specifically to meet the draft drawn by petitioner.

15. That the method of dealing between the bankrupts and the Italian Bank was no different from the method of dealing used by an ordinary
660 depositor in his bank.

16. That the bankrupts, at all times, by arrangements with the Italian Bank, retained control of all advices sent to it and could cancel such advices at any time.

17. That there is no evidence that the parties contracted or intended that the petitioner have any property right in any right the bankrupts may have had against the Italian Bank and that

the bankrupts did not sell or agree to sell any such right to the petitioner.

18. That there was no intention that the bankrupts should become a trustee for the petitioner.

19. That the bankrupts were under no obligation to create any credit in their favor and appropriate such credit for the use of the petitioner.

20. That the petitioner did not intend that it have any property right in any claim by the bankrupts against the Italian Bank.

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21. That what the petitioner wanted and what it contracted for was that funds should be available in the bank in Italy before the draft was presented and to accomplish this purpose it accepted the bankrupts' promise so to do.

22. That the petitioner has not established any equitable assignment or lien upon the bankrupts credit with the Banca Commerciale Italiana.

23. That the petitioner was not entitled to the relief demanded in the petition.

WHEREFORE, the petitioner prays the court that said exceptions to the report of the Special Master herein may be sustained. 663

FIRST NATIONAL BANK OF TRINIDAD
By O'BRIEN, BOARDMAN, PARKER & FOX,
Attorneys,
120 Broadway,
Borough of Manhattan,
City of New York.

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**Notice of Motion.**

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

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| In the Matter of OSCAR L. GUBELMAN, etc., trading as KNAUTH, NACHOD & KUHNE, etc., Bankrupts. | In Bankruptcy No. 34,996. |

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Please take notice that the undersigned will move this Court at a Stated Term thereof to be held in Room 235 of the Old Post Office Building, Borough of Manhattan, City of New York on the 4th day of March, 1925, at 10.30 o'clock in the forenoon or as soon thereafter as counsel can be heard for an order confirming Report No. 27, of the Special Master and relating to the reclamation claim of the First National Bank of Trinidad, Colo.; and for such other and further relief as to this Court seems just and proper in the premises.

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Yours, etc.,

ROSENBERG & BALL,
Attorneys for the Trustee,
74 Broadway,
Borough of Manhattan,
New York City.

To: O'BRIEN, BOARDMAN, PARKER & FOX, Esqs.,
Attorneys for the First National Bank,
of Trinidad, Colo.,
120 Broadway, New York City.

**Opinion of the District Court.**

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UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

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| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, etc., trading as KNAUTH, NACHOD & KUHNE, etc.,<br>Bankrupts. | B-34996. |
| In the Matter<br>*of*<br>THE RECLAMATION CLAIM OF THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO. | 668 |

O'BRIEN, BOARDMAN, PARKER & FOX, Esqs., attorneys for claimant, (William De Forest Manice, Allen R. Memhard, and George Trosk, of counsel).

**ROSENBERG & BALL, Esqs., attorneys for the** Trustee, (Godfrey Goldmark, George G. Ernst, and Ralph F. Colin, of counsel).

KNOX, D. J. 669

The law finally to be applied to the subject matter of this controversy between claimant and the trustee in bankruptcy of Knauth, Nachod & Kuhne will be declared by the Appellate Court, and my views concerning the same are of fleeting importance. They will not, therefore, be set forth at length. A further reason is that the Special Master has filed an elaborate and able opinion in which he reviews both the facts and the law.

670 *Opinion of the District Court.*

As to the alleged right to recover upon the first cause of action, it may be said that I believe the maximum engagement between claimant and the bankrupts to have been that the latter, in consideration of their receipt of a sum of money, merely agreed, as independent contractors, that they would provide funds or credits of their own in a designated foreign bank with which a particular draft, drawn by claimant, would, upon presentation, be paid. I do not believe that there was, as between claimants and bankrupts, a fiduciary relationship. True, the bankrupts did refer to
671 themselves as agents of the claimants

> "for the purpose of advising the issue of their drafts and providing the drawee banks with sufficient funds to cover their payment."

But agency usually implies some element of direction and control of the agent by the one who appoints him, as to the manner and method in which a particular duty shall be carried out. While the presence of such element is perhaps not always decisive of the existence of the relationship of principal and agent, it is, in this case, conspicuous by its absence.

672 Furthermore, the terms and conditions by which the bankrupts placed their "drawing service" at the disposal of inland banks, seems (aside from the designation of themselves as "agents") reasonably specific that they should act independently, and upon their own account. Any ambiguity must be resolved by the intention of the parties. Upon this, I think the position of the Trustee is supported by the facts. I cannot believe that claimant ever thought or understood that it as-

sumed any risk of loss by the bankrupts of the funds placed in their hands.

For these reasons, there can be no recovery upon the first cause of action. Favorable decision in this court upon claimant's second alleged right is foreclosed by my ruling of April 22, 1925, on the claim of Henry G. Gray in the Estate of Zimmermann & Forsbay, alleged bankrupts.

The exceptions to the report of the Special Master are overruled, and it is confirmed.

April 25, 1925.

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**Order Confirming Special Master's Report.**

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

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| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, *et al.*, trading as KNAUTH, NACHOD & KUHNE, etc.,<br>Bankrupts. | In Bankruptcy No. 34996. 675 |
| In the Matter<br>*of*<br>Reclamation Claim of FIRST NATIONAL BANK OF TRINIDAD Trinidad, Colo. | |

This matter having duly come on to be heard on March 18, 1925, upon motion of Rosenberg & Ball, attorneys for the Trustee herein, for an

676 *Order Confirming Master's Report.*

order confirming report No. 27 of the Special Master herein,

Now, upon reading and filing said report of the Special Master and the papers referred to therein and thereto annexed, and upon all of the proceedings had herein, it is, after due consideration, on motion of Rosenberg & Ball, attorneys for the Trustee herein,

ORDERED that the said report of the Special Master be and the same hereby is in all respects except as to costs and disbursements confirmed,
677 and the reclamation claim of First National Bank of Trinidad, Trinidad, Colo., be and the same hereby is dismissed; and it is

FURTHER ORDERED that the Trustee be and he hereby is authorized and directed to pay Robert P. Stephenson, as Compensation for his services as Special Master herein, $1,000.

Dated, New York, May 5, 1925.

JNO. C. KNOX,
U. S. D. J

678

**Petition for Appeal to the Circuit Court of Appeals.** 679

UNITED STATES DISTRICT COURT,

FOR THE SOUTHERN DISTRICT OF NEW YORK.

In the Matter

*of*

OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL, MARY W KNAUTH and THEODORE W. KNAUTH, doing business as co-partners under the firm name and style of KNAUTH, NACHOD & KUHNE, and OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL and THEODORE W. KNAUTH, individually, Bankrupts, 680

and

MARY W. KNAUTH, Alleged Bankrupt.

In Bankruptcy No. 34996.

In the Matter

*of*

THE RECLAMATION CLAIM OF THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO. 681

TO THE HONORABLE THE DISTRICT JUDGES OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK:

The First National Bank of Trinidad, Colorado, your petitioner, conceiving itself aggrieved by the certain order and decree in the above entitled proceeding, dated the 5th day of May, 1925, and filed in the office of the Clerk of this Court on the 5th day of May, 1925, confirming report

682 *Petition for Appeal to the Circuit Court of Appeals.*

No. 27 of Robert P. Stephenson, Special Master, dated the 19th day of February, 1925, which denied your petitioner's motion to require the Trustee herein to turn over to it the sum of $1,191.20, does hereby petition for an appeal from the said order and decree to the United States Circuit Court of Appeals for the Second Circuit, and prays that its appeal may be allowed and a citation granted directed to Middleton S. Borland, the Trustee in Bankruptcy herein, demanding him to appear before the United States Circuit Court
683 of Appeals for the Second Circuit to do and receive what may appertain to justice to be done in the premises and that a transcript of the record, proceedings and evidence in said proceeding, duly authenticated may be transmitted to the United States Circuit Court of Appeals for the Second Circuit.

Dated, New York, July 31, 1925.

FIRST NATIONAL BANK OF TRINIDAD, COLO.,
By O'BRIEN, BOARDMAN, PARKER & FOX,
Attorneys for the Petitioner,
120 Broadway,
New York City.

684 The foregoing appeal is hereby allowed.

Dated, New York, August 3rd, 1925.

JXO. C. KNOX,
U. S. D. J.

We hereby waive the filing of a bond or other undertaking for the damages and costs upon the appeal to the Circuit Court of Appeals referred to in the foregoing petition.

Dated, New York, August 3rd, 1925.

ROSENBERG & BALL,
Attorneys for Trustee.

**Notice of Appeal.** 685

## UNITED STATES DISTRICT COURT,

FOR THE SOUTHERN DISTRICT OF NEW YORK.

| | |
|---|---|
| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL, MARY W. KNAUTH, and THEODORE W. KNAUTH, doing business as co-partners under the firm name and style of KNAUTH, NACHOD & KUHNE, and OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL and THEODORE W. KNAUTH, individually,<br>Bankrupts,<br>and<br>MARY W. KNAUTH,<br>Alleged Bankrupt. | In Bankruptcy No. 34996. |
| In the Matter<br>*of*<br>THE RECLAMATION CLAIM OF THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO. | |

686

687

SIRS:

PLEASE TAKE NOTICE that the First National Bank of Trinidad, Colorado, appeals to the United States Circuit Court of Appeals for the Second Circuit to be held at the United States Court, Post Office Building, Borough of Manhattan, City of New York, from an order and decree of the United States District Court for the Southern District of New York made by Honorable John C. Knox, one of the judges thereof, dated the 5th

688 *Notice of Appeal*

day of May, 1925, and filed in the office of the Clerk of this Court on the 5th day of May, 1925, confirming the report No. 27 of Robert P. Stephenson, Special Master, dated February 19, 1925, which denied the motion of First National Bank of Trinidad, Colorado, to require the Trustee herein to turn over to it the sum of $1,191.20.

Dated, New York, August 3, 1925.

Yours, &c.,

O'Brien, Boardman, Parker & Fox,
Attorneys for Petitioner,
689 120 Broadway,
New York City.

To Messrs. Rosenberg & Ball,
Attorneys for Middleton S. Borland,
Trustee in Bankruptcy,
Knauth, Nachod & Kuhne,
74 Broadway,
New York City.

Alexander Gilchrist, Jr., Esq.,
Clerk of the U. S. District Court,
for the Southern District of New York.

690

## Citation on Appeal.

691 By the Honorable John C. Knox, one of the United States District Court Judges for the Southern District of New York, in the Second Circuit.

To Middleton S. Borland, Trustee in Bankruptcy of Oscar L. Gubelman, Rollin C. Newton, James F. Shaw, Herbert B. Smithers, John R. Hall, Mary W. Knauth and Theodore W. Knauth, doing business as co-partners under the firm name and style of Knauth, Nachod & Kuhne, and Oscar L. Gubelman, Rollin C. Newton, James F. Shaw, Herbert B. Smithers, John R. Hall and Theodore W. Knauth, individually, Greeting.

692 You are hereby cited and admonished to be and appear before a United States Circuit Court of Appeals for the Second Circuit, to be holden at the Borough of Manhattan in the City of New York, in the District and Circuit above named on the 1st day of September, 1925, pursuant to an appeal filed in the Clerk's Office of the District Court of the United States for the Southern District of New York, wherein you as trustee in bankruptcy of the above named bankrupts are appellee, and the First National Bank of Trinidad, Colorado, is the appellant, and you are ordered to show cause, if any there be, why the order and decree in said appeal mentioned should not be 693 corrected and why speedy justice should not be done to the parties in that behalf.

Given under my hand at the Borough of Manhattan, in the City of New York, in the District and Circuit above named this 3rd day of August, in the year of our Lord One Thousand Nine Hundred and Twenty-five, and of the Independence of the United States the One Hundred and Fiftieth.

Jno. C. Knox,
United States District Judge for the Southern District of New York, in the Second Circuit.

694 **Assignment of Errors.**

UNITED STATES DISTRICT COURT,

FOR THE SOUTHERN DISTRICT OF NEW YORK.

| | |
|---|---|
| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL, MARY W. KNAUTH and THEODORE W. KNAUTH, doing business as co-partners under the firm name and style of KNAUTH, NACHOD & KUHNE, and<br>695 OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL and THEODORE W. KNAUTH, individually,<br>Bankrupts,<br>and<br>MARY W. KNAUTH,<br>Alleged Bankrupt. | In Bankruptcy No. 34996. |
| In the Matter<br>*of*<br>THE RECLAMATION CLAIM OF THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO. | |

696 Now comes the First National Bank of Trinidad, Colorado, the appellant herein, and files the following assignment of errors on appeal from an order of this Court dated May 5th, 1925, complaining as follows:

1. The Court erred in matter of law in finding that the contract between your petitioner and the bankrupts did not constitute the bankrupts the agents of your petitioner for the transmission to foreign

countries of funds delivered to the bankrupts by petitioner. 697

2. The Court erred in matter of law in finding that the bankrupts were not trustees for the petitioner of the moneys delivered to them by petitioner.

3. The Court erred in matter of law in holding that there was no fiduciary relationship between petitioner and bankrupts.

4. The Court erred in matter of law in finding that there had not been an equitable assignment of the fund in question by Banca Commerciale Italiana. 698

5. The Court erred in matter of law in finding that petitioner by availing itself of the bankrupts "Drawing Service" never agreed to assume any risk of loss by the bankrupts of the funds placed in the bankrupts hands.

6. The Court erred in matter of law in finding that petitioner was not entitled to recover as prayed by it.

7. The Court erred in matter of law in overruling petitioner's exceptions to the report of the Special Master herein and in confirming said report. 699

WHEREFORE appellant prays that said order and decree herein for the manifest errors aforesaid and for the other errors in the records and proceedings herein may be reversed and that the United States District Court for the Southern District of New York may be directed to enter

700 *Assignment of Errors.*

an order and decree herein granting the amended petition of appellant dated the 20th day of October, 1924, and brought on by notice of hearing dated the 29th day of August, 1924, and directing the Trustee in Bankruptcy herein to pay to appellant the sum of $1,191.20, together with its costs and disbursements herein.

Dated, July 31, 1925.

FIRST NATIONAL BANK OF TRINIDAD, COLO.,
By O'BRIEN, BOARDMAN, PARKER & FOX,
Attorneys for Appellant,
701 120 Broadway,
New York City.

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703

**Notice of Filing Petition to Revise.**

UNITED STATES DISTRICT COURT,

FOR THE SOUTHERN DISTRICT OF NEW YORK.

| | |
|---|---|
| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL, MARY W KNAUTH and THEODORE W. KNAUTH, doing business as co-partners under the firm name and style of KNAUTH, NACHOD & KUHNE, and OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL and THEODORE W. KNAUTH, individually, Bankrupts,<br>and<br>MARY W. KNAUTH,<br>Alleged Bankrupt. | In Bankruptcy No. 34996. |
| In the Matter<br>*of*<br>THE RECLAMATION CLAIM OF THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO. | |

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SIRS:

PLEASE TAKE NOTICE that on the 31st day of July, 1925, at 10:30 o'clock, we shall file in the Clerk's Office of the United States Circuit Court of Appeals for the Second Circuit, in the City of New York, a petition for review in the above en-

706 *Notice of Filing Petition to Revise.*

titled cause, a copy of which petition is annexed hereto and made a part of this notice.

Dated, New York, July 28th, 1925.

Yours, &c.,

O'BRIEN, BOARDMAN, PARKER & FOX,
Attorneys for Petitioner,
120 Broadway,
New York City.

To ROSENBERG & BALL,
Attorneys for Trustee,
707 74 Broadway,
New York City.

708

**Petition to Revise.** 709

UNITED STATES DISTRICT COURT,

FOR THE SOUTHERN DISTRICT OF NEW YORK.

| | |
|---|---|
| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, ROLLIN C. NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL, MARY W KNAUTH and THEODORE W. KNAUTH, doing business as co-partners under the firm name and style of KNAUTH, NACHOD & KUHNE, and OSCAR L. GUBELMAN, ROLLIN C NEWTON, JAMES F. SHAW, HERBERT B. SMITHERS, JOHN R. HALL and THEODORE W. KNAUTH, individually, Bankrupts,<br>and<br>MARY W. KNAUTH, Alleged Bankrupt. | 710<br>In Bankruptcy No. 34996. |
| In the Matter<br>*of*<br>THE RECLAMATION CLAIM OF THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO. | |

TO THE HONORABLE JUDGES OF THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT: 711

Your petitioner, the First National Bank of Trinidad, Colorado, appearing by O'Brien, Boardman, Parker & Fox, its attorneys, respectfully shows:

I.—That it is a corporation, duly organized under and by virtue of the National Banking

Laws of the United States, having its principal place of business in the City of Trinidad, in the State of Colorado.

II.—That the above named copartnership of Knauth, Nachod & Kuhne, consisting of Oscar L. Gubelman, James F. Shaw, Rollin C. Newton, Herbert B. Smithers, John R. Hall, Mary W. Knauth and Theodore W. Knauth, were duly adjudged bankrupts under the Acts of Congress relating to Bankruptcy by the United States District Court for the Southern District of New York
713 on the 12th day of January, 1924. That the said Oscar L. Gubelman, James F. Shaw, Rollin C. Newton, and John R. Hall, individually, were duly adjudged bankrupts under the Acts of Congress relating to Bankruptcy by the United States District Court for the Southern District of New York on the said 12th day of January, 1924, and and that the said Herbert B. Smithers and Theodore W. Knauth, individually, were duly adjudged bankrupt under the Acts of Congress relating to bankruptcy by the United States District Court for the Southern District of New York on the 1st day of February, 1924, and that the said Mary W. Knauth, individually, was duly adjudged
714 bankrupt under the Acts of Congress relating to bankruptcy by the United States District Court for the Southern District of New York on the 9th day of January, 1925.

III.—That the following proceedings were had in the case of the said bankrupts:

By order of the United States District Court, dated the 23rd day of April, 1924, all creditors of the above named bankrupts claiming specific money, bonds, stocks, certificates or other prop-

erty or any interest therein or the proceeds thereof in the possession of the Receiver, or which might come into his possession, were directed to file proofs of claim in and to said specific moneys, bonds, stocks, certificates or other money in the office of Robert P. Stephenson, Esq., as Special Master, on or before June 19th, 1924. Pursuant to said order, your petitioner filed its petition herein, verified the 19th day of June, 1924, in the office of Robert P. Stephenson, as Special Master, and subsequently by order of the United States District Court, dated the 15th day of October, 1924, an amended petition, verified the 20th 716
day of October, 1924, was duly filed in the office of the said Robert P. Stephenson, Special Master. That the said amended petition was for an order directing the Trustee in Bankruptcy herein to pay over to your petitioner the sum of $1,191.20 being moneys paid by your petitioner to the bankrupts under the "Drawing Service" of the said bankrupts for the purpose of paying a draft drawn by your petitioner under the said "Drawing Service" upon the Banca Commerciale Italiana, Italy, and which said money, subsequent to the filing of the petition in bankruptcy came into the possession of the Receiver in Bankruptcy and
subsequently into the possession of the Trustee in 717
Bankruptcy. That after the taking of testimony upon said petition a report was made by the said Special Master dated the 19th day of February, 1925, denying your petitioner's motion and dismissing its petition. That a motion was made to the United States District Court for the Southern District of New York to confirm the said report of the Special Master, which motion, upon notice, came on for hearing before the United States District Court for the Southern District of New York

718 *Petition to Revise.*

on the 18th day of March, 1925, and on the 5th day of May, 1925, an order was made by the said District Court affirming the said order of the Special Master of February 19th, 1925, a copy of which order of the said District Court is hereto annexed and marked Exhibit "A."

IV.—That said order was erroneous in matter of law in that—

1. The Court erred in matter of law in finding that the contract between your petitioner and the bankrupts did not consti-
719 tute the bankrupts the agents of your petitioner for the transmission to foreign countries of funds delivered to the bankrupts by petitioner.

2. The Court erred in matter of law in finding that the bankrupts were not trustees for the petitioner of the moneys delivered to them by petitioner.

3. The Court erred in matter of law in holding that there was no fiduciary relationship between petitioner and bankrupts.

4. The Court erred in matter of law in
720 finding that there had not been an equitable assignment of the fund in question by Banca Commerciale Italiana.

5. The Court erred in matter of law in finding that petitioner by availing itself of the bankrupts "Drawing Service" never agreed to assume any risk of loss by the bankrupts of the funds placed in the bankrupts' hands.

6. The Court erred in matter of law in

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finding that petitioner was not entitled to recover as prayed by it.

7. The Court erred in matter of law in overruling petitioner's exceptions to the report of the Special Master herein and in confirming said report.

WHEREFORE your petitioner, feeling aggrieved because of such order, asks that the same be reviewed, revised and reversed in matter of law by your Honorable Court, as provided in Section 24b of the Bankruptcy law of 1898, and the Rules and Practice in such case provided.

722

Dated, July 28th, 1925.

FIRST NATIONAL BANK OF TRINIDAD, COLO.,
Petitioner.

O'BRIEN, BOARDMAN, PARKER & FOX,
Attorneys for Petitioner,
Office and Post Office Address,
120 Broadway,
New York City.

STATE OF NEW YORK,
County of New York, } ss.:

723

ERNEST R. EARLY, being duly sworn, deposes and says: that he is a member of the firm of O'Brien, Boardman, Parker & Fox, 120 Broadway, New York City, the attorneys for the petitioner herein; that he has read the foregoing petition and knows the contents thereof and that the same is true to his knowledge.

Deponent further says that the reason why this verification is not made by petitioner and is made by him is that the petitioner is a foreign corpora-

724 *Petition to Revise.*

tion which does not maintain an office or agent in the City of New York.

ERNEST R. EARLY.

Sworn to before me this
28th day of July, 1925.

WILLIAM H. VOGT,
[NOTARIAL SEAL] Notary Public,
Queens County.

Queens County No. 1154.
Certificate filed in New York Co.
New York C. Clerk's No. 114.
New York Co. Register's No. 8086.
725 Commission expires March 30, 1926.

**Exhibit "A."**

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

| | |
|---|---|
| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, *et al.*, trading as KNAUTH, NACHOD & KUHNE, etc.,<br>Bankrupts. | In Bankruptcy No. 34996. |
| 726 In the Matter<br>*of*<br>Reclamation Claim of FIRST NATIONAL BANK OF TRINIDAD, TRINIDAD, COLO. | |

This matter having duly come on to be heard on March 18, 1925, upon motion of Rosenberg &

727

Ball, attorneys for the Trustee herein, for an order confirming report No. 27 of the Special Master herein, Now, upon reading and filing said report of the Special Master and the papers referred to therein and thereto annexed, and upon all of the proceedings had herein, it is, after due consideration, on motion of Rosenberg & Ball, attorneys for the Trustee herein,

ORDERED that the said report of the Special Master be and the same hereby is in all respects except as to costs and disbursements confirmed, and the reclamation claim of FIRST NATIONAL BANK OF TRINIDAD, TRINIDAD, COLO., be and the same hereby is dismissed; and it is

728

FURTHER ORDERED that the Trustee be and he hereby is authorized and directed to pay Robert P. Stephenson, as Compensation for his services as Special Master, herein, $1,000.

Dated, New York, May 5, 1925.

JNO. C. KNOX,
U. S. D. J.

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**Stipulation Combining Record.**

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

| | |
|---|---|
| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, etc., trading as KNAUTH, NACHOD & KUHNE, etc.,<br>Bankrupts. | In Bankruptcy No. 34,996. |

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It is hereby stipulated by and between the parties hereto that the record on the appeal and the petition to revise herein may be combined and printed together and that the one record may be used in both proceedings.

Dated, New York, August 10, 1925.

O'BRIEN, BOARDMAN, PARKER & FOX,
Attorneys for Appellant.

ROSENBERG & BALL,
Attorneys for Respondent.

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**Stipulation as to Record.**

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

| | |
|---|---|
| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, etc., trading as KNAUTH, NACHOD & KUHNE, etc.,<br>Bankrupts. | In Bankruptcy No. 34,996. |

734

It is hereby stipulated and agreed that the foregoing is a true transcript of the Record of the United States District Court in the above entitled matter as agreed upon by the parties.

Dated, New York, August , 1925.

O'BRIEN, BOARDMAN, PARKER & FOX,
Attorneys for Reclaimant.

ROSENBERG & BALL,
Attorneys for Middleton S. Borland, Trustee in Bankruptcy.

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## Clerk's Certificate.

UNITED STATES DISTRICT COURT,

SOUTHERN DISTRICT OF NEW YORK.

| | |
|---|---|
| In the Matter<br>*of*<br>OSCAR L. GUBELMAN, etc., trading as KNAUTH, NACHOD & KUHNE, etc.,<br>737 Bankrupts. | In Bankruptcy No. 34,996. |

I, ALEXANDER GILCHRIST, JR., Clerk of the District Court of the United States for the Southern District of New York, do hereby certify that the foregoing is a correct transcript of the Record of the said District Court in the above entitled matter as agreed on by the parties.

IN WITNESS WHEREOF I have caused the seal of the said Court to be hereunto affixed in the City of New York, Southern District of New York, this day of , 1925.

738 ALEXANDER GILCHRIST,
Clerk.

# UNITED STATES CIRCUIT COURT OF APPEALS

FOR THE SECOND CIRCUIT.

No. 155—October Term, 1925.

Argued November 18, 1925. Decided July 6, 1926.

In Re

OSCAR L. GUBELMAN and others,

*Ex parte*

THE FIRST NATIONAL BANK OF TRINIDAD, 740

Appellant,

MIDDLETON S. BORLAND, Trustee,

Appellee.

PETITION TO REVISE ORDER OF THE DISTRICT COURT OF THE UNITED STATES FOR THE SOUTHERN DISTRICT OF NEW YORK.

Before ROGERS, MANTON and HAND, Circuit Judges.

Appeal from an order of the District Court for 741
the Southern District of New York confirming the report of a special master disallowing priority in bankruptcy to a claim of the petitioner.

The bankrupts were international bankers doing business in the City of New York. A part of their business consisted in making contracts with country banks by which such banks might, with certainty that they would be honored, sell drafts to their customers drawn upon foreign banks, correspondents of the bankrupts. These

contracts read as follows: "Upon receipt of advice of draft accompanied by adequate funds payable at par in New York we," the bankrupts, "shall (sic) promptly forward our advice of the same and provide the drawee with funds sufficient for the payment of the draft abroad, or* a transfer of credit from our balance or otherwise. * * * In other words, we are employed merely as the agents of the drawers for the purpose of advising the issue of drafts and providing the drawee banks with sufficient funds to cover their pay-
743 ment."

In accordance with such a contract, the petitioner, a country bank, on May nineteenth, 1923, drew upon the Sassari branch of the Banca Commerciale Italiana for 24,360 lire in favor of one, Zara Sanna Giovanni. On the same day it advised the bankrupts of the draft in the following language, which the bankrupts had prescribed in the forms accompanying the contract: "Pursuant to the terms and conditions governing your drawing service we have sold draft bearing the above number, dated Trinidad, Colorado, May 19, 1923, for Lir. 24,360 and shall thank you to pro-
744 tect same upon presentation. We remit herewith the sum of $1,191.20." This advice was accompanied by a cheque covering the draft in question and another. The bankrupts cashed the cheque and on the twenty-second wrote to the drawee as follows: "Please protect to the debit of our account the drafts as per particulars." Among such particulars were several drafts drawn upon the drawee's Sassari branch, includ-

*The word "or" should be "by". See Record, page 141, folio 422.

745

ing by specific description the draft in question.

The bankrupts had on deposit with the drawee funds sufficient to cover the drafts so advised, against which the drawee debited the drafts and stopped interest upon the amount so debited. It made a corresponding credit at the same time in an account entitled, "drafts payable." Both entries were made before petition filed, and were in accordance with a standing agreement between the bankrupts and the drawee.

The draft was presented for payment after petition filed and was dishonored. Thereafter the 746
receiver procured from the drawee a reversal of the charge on its books against the bankrupts, of the credit in favor of the draft in the account, "drafts payable," and a remittance of the restored deposit. The petitioner as drawer was compelled to take up the draft after dishonor, and now presents its claim as a preferred creditor, on the ground among others that the holder of the draft had become an equitable assignee of the bankrupts' deposit with the drawee. The trustee, who succeeded below, admits the right of the petitioner as general creditor, but denies the priority.

747
The trustee also relied upon a custom which obtained in business done under such an arrangement. If the correspondent of the foreign drawee wished to cancel a draft, he might so advise the drawee, who would thereupon reverse the credits and remit the deposit or make such other disposition as was directed. The correspondent might be himself the drawer, or have the relation to the draft of the bankrupts. The only instances of the practise known to the witnesses were those

748 *Opinion.*

in which the draft had been already cancelled, or at least when it was not outstanding in the hands of a holder in due course.

William D. Manice, Allen R. Memhard and George Trosk, all of New York City, for the petitioner-appellant.

Godfrey Goldmark, George G. Ernst and Ralph F. Colin, all of New York City, for the trustee below.

Logan Hay and Sidney Wetmore
749 Davidson, of New York City, as *amici curiae* for parties similarly interested.

Hand, Circuit Judge (after stating the facts as above):

It does not seem necessary to us to decide whether the bankrupts remained liable upon the draft after they had posted the advice to the drawee and the drawee had made the necessary entries on its books. Even if they did so remain, they could so finally and completely devote a part of their balance with the drawee to the payment
750 of the draft as to create themselves constructive trustees pro tanto for the benefit of the holder, and disable themselves thereafter from recalling what they had done. Performance once executed was irrevocable, because there was no intimation of any right to revoke it, and because the continued liability of the bankrupts was not an equivalent of performance, as the event proved. An obligee is not exposed to the renewed hazard of performance, once the obligor has performed, nor may the obligor at his whim undo that which

he once did in satisfaction of his promise. For the moment we reserve any difference which the supposed custom might create.

It is, however, proper to observe that if, as we think, the bankrupts did not remain liable after performance, their action in advising the drawee to transfer the credits was more plainly a final appropriation of the deposit than it would otherwise have been. On such a view by those acts they had acquitted themselves of all their obligations and certainly the contract intended that they should secure payment of the draft. If they secured it at all, it must have been when they did 752
the last necessary act. As a make-weight, therefore, we give our reasons for saying that the limit of their obligation was to secure the entries upon the drawee's books. If they had meant to become guarantors, the relation and the word were familiar enough, and it seems to us incredible that they should not have said so more unequivocally. Instead, they used language which cannot by any stretch be confused with a guaranty; their only undertaking was to advise the drawee, and to put him in funds. They expressly liimted their employment "merely as agents of the drawees' for these purposes. Again, on the 753
cover of the form-book which the trustee at least insists was a part of the contract these were said to be their "sole function." How it can be thought that the bankrupts remained any longer liable, once the drawee set up the credit in favor of the holder, we cannot understand. That was the whole of their stipulated performance, and there is no room for implications.

The trustee replies by insisting upon the language of the drawer's advice when remitting the

covering funds; "we shall thank you to protect" the draft. Although that phrase was selected by the bankrupts, it will not serve to avoid the contract itself. "Protect" may indeed in other contexts mean "guaranty," but not in this. We are to make the whole language read consistently, and if "protect" means "guaranty," the "mere employment" as, and the "sole function" of, a remitting agent must be consistent with assuming absolute responsibility for the payment of the draft. Certainly they are not. On the other hand it does not wrench the word to say that the
755 drafts are protected when the drawees are put in funds. We have no evidence that the bankrupts' profit was adequate for any larger responsibility, but if it was, none was assumed.

With this conclusion as a background we have to consider whether the contract and the action under it created an equitable assignment. It is of course true that a cheque or draft is not an assignment of funds on deposit with the drawee, though there is respectable authority to the contrary. It is not entirely clear why on principle the holder should not be allowed to sue upon the drawee's general promise to the drawer to honor
756 his orders. Perhaps as Mr. Williston says, (*Williston on Contracts*, Sec. 389), closely considered, the drawee is only the drawer's agent to pay, yet even so, the promise of an agent is as binding as anyone's else and it seems rather hard to escape the conclusion that the drawee has promised to honor drafts so long as he remains in funds. For whatever reasons courts have gone far to find indications in such cases of an independent agreement to assign an interest in the funds. The

most conspicuous case was *Fourth Street Bank* vs. *Yardley*, 165 U. S., 634, 17 S. Ct. 439, 41 L. Ed., 855, where the agreement was spelled out from circumstances far less cogent than those at bar. Similar instances are *Farley* vs. *Turner*, 26 L. J. Chan., 710; *Burns* vs. *Carvalho*, 4 Milne & Craig, 690; *Coates* vs. *First National Banks*, 91 N. Y., 20; *Muller* vs. *Kling*, 209 N. Y., 239, 103 N. E., 138; *In re Hollins*, 215 F. 41, 131 C. C. A., 349, L. R. A. 1915 B, 438 (C. C. A. 2). The rule is but an illustration of the general principle that an executory agreement may create such a right, if it 758
plainly enough indicates a purpose to appropriate specific property for the payment of a debt, *Walker* vs. *Brown*, 165 U. S., 654, 17 S. Ct., 453, 41 L. Ed., 865; *Ingersoll* vs. *Coram*, 211 U. S., 335, 29 S. Ct., 92, 53 L. Ed., 208; *Hurley* vs. *Atchison etc. R. R.*, 213 U. S., 126, 29 S. Ct., 466, 53 L. Ed., 729; *Parlin etc. Co.* vs. *Moulden*, 228 F., 111, 142 C. C. A., 517, L. R. A. 1917 B, 130, (C. C. A. 5); *Curtis* vs. *Walpole etc. Co.*, 218 F., 145, 134 C C. A., 140, (C. C. A. 1). As in the case of a trust, with which it is closely allied, the intent depends upon the form of the transaction and is necessarily subject to no exact test, *Steel Cities* 759
*Chem. Co.* vs. *Va. Car. Chem. Co.*, 7 F., (2d), 280, (C. C. A. 2); *Rogers Locomotive Works* vs. *Kelley*, 88 N. Y., 234.

The contract in the case at bar clearly contemplated a final appropriation of the deposit, for the benefit of the holder of the draft. The phrase, "transfer of credit", could only have meant a cancellation of the bankrupts' interest in their balance and an establishment of a corresponding

credit in favor of the holders of the drafts. The action taken by the drawee was, *prima facie* at any rate, consistent only with that purpose. We are of course aware that entries upon bankers' books are not conclusive evidence of a completed transaction. *In re Gubelman, ex parte Latzko & Popper,* 10 F. (2d), 926, (C. C. A. 2). But they are none the less probative. If the bankrupts had had no balance with the drawee but had remitted funds specifically to cover the draft, we can hardly suppose that it would be argued
761 that these were not specifically attributed to the benefit of the holders, and available to them. Yet the contract treats that situation as an alternative to the transfer of credit. It cannot be that what was a final appropriation in one case was not in the other. Therefore, it seems to us that the agreement to transfer the credit, followed by its actual transfer, provided a fund which the drawee was obliged to devote to the payment of the draft, that is, that it created an equitable assignment or an irrevocable declaration of trust by the bankrupts.

The cases relied on by the trustee are not con-
762 trolling. In *Eastman Kodak Co.* vs. *National Park Bank* (D. C.), 231 F. Rep., 320 and 247 F. 1002, 159 C. C. A. 662 (C. C. A. 2), the drawee had not transferred the credits and so far as appeared, remained free to pay the drafts in the order of their presentation. Mere notice by the drawer does not establish a priority upon the fund in favor of the drafts advised. It is a vital difference when the drawee by specific credits provides for specific drafts. These must then be

paid, no matter how many others come in before them, and that implies a final appropriation *pro tanto*. Our decision in *Re Interborough Consolidated Corp.*, 288 F. 334, 32 A. L. R. 932, is quite remote. There, the mortgagor did not establish a credit on which the bondholders might draw, but drew cheques itself t opay the coupons. More nearly akin is *Noyes* vs. *First National Bank*, 180 App. Div., 162, 167 N. Y. S. 288, affirmed 224 N. Y., 542, 120 N. E. 870, where the bondholders presented their coupons direct to the disbursing agent who paid them itself. However, the funds 764
were not credited to the bondholders on the books of the agent. On the contrary, we think that they were credited, perhaps somewhat ambiguously, as an account of the debtor, though for its convenience the ultimate destination of the money appeared in the title. In the first place we are not prepared to agree that there is no difference between a payment made by the debtor at its agent's office and a payment made by the drawee of a draft. But even if there be none, there is a wide distinction between an account of the debtor, however, tagged or ear-marked, and a transfer of credit from the debtor to the creditor. *Erb* vs. *Banco di Napoli* (May 25, 1926), 243 N. Y. 45, 765
152 N. E. 460 adds nothing to Noyes's case.

The law in New York apparently is otherwise in respect of dividends, *LeRoy* vs. *Globe Ins. Co.*, 2 Edw. Ch. 657; *In re Le Blanc*, 14 Hun 8, affirmed 75 N. Y., 598, *In re Interborough Consolidated Corp.* (D. C.), 267 F. 914. The distinction is not very clear because a dividend once declared is a debt, but unless the later cases have over-

ruled the earlier, it is only fair to say that Noyes's case must be regarded as close to the line.

There remains the question of custom. The evidence went no further than to show a practise of reversing the credits when the draft was cancelled. That was natural enough, but it is quite another thing to do so while the draft is outstanding. A custom which should allow the rights of a holder to be so changed, once they had become fixed in accordance with contracts made in his interest, ought to be proved by the most cogent evidence, if it could be valid at all. There was
767 not even an intimation that it went so far.

The last point is that in the absence of any proof of Italian law we cannot say what was the legal consequence of the entries made by the drawee in Italy. If the case involved the holder's rights against the drawee upon the deposit that might be true, but it does not. The question is whether the bankrupts made themselves constructive trustees of their claim against the drawee; that quesion depends upon the law of the place where the supposed trustees acted. We cannot regard the making of the entries as the declaration of trust, even though without them the ap-
768 propriation would have been incomplete. The bankrupts' fiduciary relation to the deposit was created by the contract, and by their appropriation of their funds to the benefit of the holder. These took place here. The drawee's compliance with their orders was at most only a condition, and the law of the place where the condition was fulfilled did not determine the effect of the declaration, but the law of the place where the declaration itself was made.

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In view of the foregoing discussion it is unnecessary to consider the petitioner's first point, i. e., whether the bankrupts originally received the petitioner's cheque in a fiduciary capacity.

The order is reversed and the cause is remanded with instructions to grant the petitioner a priority in its claim.

Rogers, Circuit Judge, because of illness, has been unable to take part in this decision.

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**Judgment.**

At a Stated Term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the Court Rooms in the Post Office Building in the City of New York, on the 13th day of July one thousand nine hundred and twenty-six.

Present—Hon. Henry Wade Rogers,
Hon. Martin T. Manton,
Hon. Learned Hand,
773 Circuit Judges.

In the Matter

*of*

Oscar L. Gubelman, *et al.*, trading as Knauth, Nachod & Kuhne, etc.,

Bankrupts,

First National Bank of Trinidad, Colorado,

774 Petitioner.

Petition to Revise Order of the District Court of the United States for the Southern District of New York.

This cause came on to be heard on the transcript of record from the District Court of the United States, for the Southern District of New York, and was argued by counsel.

*Judgment.* 775

On Consideration Whereof, It is now hereby ordered, adjudged, and decreed that the order of the said District Court be and it hereby is reversed with costs, and cause remanded with instructions to grant the petitioner a priority in its claim.

It is further ordered that a Mandate issue to the said District Court in accordance with this decree.

M. T. M.
L. H.

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United States of America, }
Southern District of New York, } ss.:

I, William Parkin, Clerk of the United States Circuit Court of Appeals for the Second Circuit, do hereby Certify that the foregoing pages, numbered from 1 to 252 inclusive, contain a true and complete transcript of the record and proceedings had in said Court, in the case of

In the matter of Oscar L. Gubelman et al., trading as Knauth, Nachod & Kuhne, etc.,

Bankrupts, 777

First National Bank of Trinidad, Colorado,

Petitioner.

as the same remain of record and on file in my office.

778 *Judgment.*

In Testimony Whereof, I have caused the seal of the said Court to be hereunto affixed, at the City of New York, in the Southern District of New York, in the Second Circuit, this 5th day of August in the year of our Lord One Thousand Nine Hundred and twenty-six and of the Independence of the said United States the One Hundred and Fifty-first.

(signed) William Parkin,
[seal] Clerk.

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Supreme Court of the United States

Order Allowing Certiorari—Filed November 23, 1926

**The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.**

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Office Supreme Court, U. S.
FILED
SEP 29 1926
WM. R. STANSBURY
CLERK

No. [redacted] 180

# Supreme Court of the United States

OCTOBER TERM—1926.

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THE EQUITABLE TRUST COMPANY OF NEW YORK as Trustee in Bankruptcy of Knauth, Nachod & Kuhne,

*Petitioner,*

*against*

THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO,

*Respondent.*

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## PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, AND BRIEF IN SUPPORT THEREOF.

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GODFREY GOLDMARK, ESQ.,
*Counsel for Petitioner,*
74 Broadway,
New York City,
New York.

## SUBJECT INDEX.

### Petition.


| | PAGE |
|---|---|
| Nature of Proceeding and Decision Below | 1 |
| Statement of Salient Facts | 2 |
| The Contentions of Petitioner-Trustee | 4 |
| The Basis of the Court's Decision Contrary to the Uncontradicted Evidence as to History and Purpose of "Drafts Payable Account" | 5 |
| The Decision in the Zimmerman & Forshay case | 7 |
| The Fundamental Errors of the Court Below | 8 |
| Important Reasons Why this Court Should Grant the Writ | 9 |
| Conflict in Decisions | 11 |
| Verification | 12 |
| Certificate of Counsel | 12 |
| Appendix A—Opinion in Zimmerman case | 13 |


### Brief of the Argument.


| | |
|---|---|
| Detailed Statement of Facts Showing the Successive Steps in the Transactions Between the Parties | 15 |
| Holdings Below | 18 |
| Brief of the Argument | 19 |
| POINT I—Neither the Contract of the Parties nor any of the Acts Done by K. N. & K. or the B. C. I. After the Receipt of the American Dollars Were Intended To Constitute or Did Constitute an Equitable Assignment of K. N. & K.'s Balance in the B. C. I. as Claimed by the Respondent | 20 |

PAGE

POINT II—Because of the International Banking Practice and Because the Holder of the Draft (to whose Rights the Court Below Held the Respondent Subrogated) Had No Notice of the Alleged Assignment and Did Not Consent Thereto, Any Alleged Assignment Was Revocable and the Balance Assigned Remained Subject to the Bankrupts' Control, and Accordingly Was Property Which Passed to the Trustee Under Section 70a (3) (5) of the Bankruptcy Act ..... 42

POINT III—There Initially Was No Trust Relationship and the Parties Dealt as Independent Contractors ..... 43

POINT IV—The Petition for a Writ of Certiorari Should Be Granted ..... 44

---

## TABLE OF AUTHORITIES.

Aetna Nat'l Bk. vs. Fourth Nat'l Bk., 46 N. Y., 82 ..... 24
Bankruptcy Act, Section 70a (3) and (5) ..... 42
Beecher vs. Cosmopolitan Trust Co., 239 Mass., 48 ..... 43
Casement vs. Brown, 148 U. S., 615 ..... 44
Christmas vs. Russell, 14 Wall, 69 ..... 23, 24
Cushings vs. Chapman, 115 Fed., 237 ..... 23
Eastman Kodak Company vs. Park Nat'l Bk., 231 Fed., 320 ..... 23, 24
Erb vs. Banco di Napoli, 243 N. Y., 45 ..... 11
Gravenhorst vs. Zimmerman, 236 N. Y., 22 ..... 44
Hamer vs. Sidway, 124 N. Y., 538 ..... 21
Interborough Consolidated Corp., Re, 228 Fed., 334 ..... 11, 21, 22
Kuehne vs. Union Trust Co., 133 Mich., 602 ..... 25
Legniti vs. Mech. & Metals Nat'l Bk., 230 N. Y., 415 ..... 43

PAGE

Nat'l City Bk. vs. Hotchkiss, 231 U. S., 50..... 24
Noyes vs. First National Bank, 180 App. Div., 162 11, 24
Pomeroy, Eq. Jur. (Fourth Ed.) Sec. 1281-1284 9, 21, 24, 42
Samuels vs. E. F. Drew & Co., 296 Fed., 882..... 44
Sloan Shipyards Corporation vs. Fleet Corp., 258 U. S., 549 ..... 44
Spellman vs. Bankers Trust Co., 6 Fed. (2nd), 799.. 21
Stiger, In re, 202 Fed., 791..... 23
Taussig vs. Carnegie Trust Co., 156 App. Div., 519.. 25
Tiernan vs. Jackson, 5 Peters, 579 ..... 22
Wabash R. R. vs. Ham, 114 U. S., 587..... 5
Williams vs. Everett, 14 East., 581..... 22
Williams vs. Ingersoll, 89 N. Y., 508..... 24
Zimmerman & Forshay, Matter of (unreported)....7, 13

The case presents for determination the rights of the parties to an international banking and exchange transaction of a kind conducted daily in great number in the financial centers of the country and involving millions of dollars yearly. The Trinidad Bank claim is similar to approximately two hundred and twenty claims filed by other banks and bankers in the bankruptcy proceeding and involving approximately $850,000. It is hoped that the determination of this claim will make unnecessary the separate trial of each of the other individual reclamation claims.

## II.

### Statement of Salient Facts.

The reclaimant respondent (as well as the other reclaimants whose petitions are similar to that of this respondent) seeks to recover either a fund alleged to have been remitted by the respondent to the bankrupts in trust for a special purpose, or a fund transmitted to the Receiver in bankruptcy by foreign depositaries of the bankrupts, which fund it is claimed had been equitably assigned to the respondent or its predecessor in interest. That claim arises from the following facts:

The bankrupts maintained balances with numerous foreign banks. Thousands of banks throughout the country (hereinafter referred to as inland banks) had no balances abroad, but desired facilities under which such inland banks would be enabled to draw drafts or issue money orders *in their own name* upon foreign banks in which such inland banks maintained no balances. These facilities were supplied to the inland banks by a "drawing service" maintained by the bankrupts.

Under the "drawing service," which in its essentials was similar to that offered to inland banks by various other New York banking institutions, the procedure was substantially as follows:

The inland bank would draw its own draft in a foreign currency upon a foreign bank (in which it had no balance) and would issue that draft to its customer. The name of the bankrupts did not appear on the draft. The inland bank would then advise the bankrupts that it had drawn the draft and would ask the bankrupts to "protect" the draft upon its presentation. Said request was accompanied by a payment to the bankrupts in American dollars calculated at exchange rates furnished daily by the bankrupts. Upon receipt of such request and payment, the bankrupts deposited the money received in their general domestic bank account—in the Trinidad case, the Guaranty Trust Company—and sent written advices by mail to the drawee bank upon which the inland bank had issued its draft. Said advice requested the foreign bank to honor the draft issued by the inland bank "charging same" to the bankrupt's account with that foreign bank.

Immediately upon receipt of said advice and before the presentation of the draft for payment, the foreign drawee bank charged the bankrupt's account for the amount of the draft and credited that amount to an account on its books termed "Drafts Payable." However the testimony showed without contradiction that the bankrupts retained control of the amount so credited and that the foreign bank recognized their right to cancel such advices.

At the time of the filing of the petition in bankruptcy there were outstanding innumerable drafts, thus drawn by inland banks and advised and charged in the "Drafts Payable" account, which had not been presented to the foreign banks for payment by the payees or holders thereof. Immediately upon the appointment of the Receiver the advices of outstanding drafts were cancelled by the Receiver and the balances in the "Drafts Payable" account were eventually remitted to the Trustee.

It is against the fund so returned or against the bank

rupts' balance with the Guaranty Trust Company (which balance was also paid over to the Trustee) that the inland bank, the respondent here, has filed its reclamation claim. That is, the claim was filed on two theories—either that the funds received by the bankrupts from the inland bank and deposited in the Guaranty Trust Company were received in a fiduciary capacity; or that the transaction outlined above resulted in an equitable assignment of the balance which was credited to the "Drafts Payable" account abroad and that that fund, having been returned to the Trustee, can be reclaimed.

The Special Master held that there was neither an initial trust nor an equitable assignment and his decision was confirmed by the District Court. The Circuit Court of Appeals reversed the latter decision and held that there was an equitable assignment of the foreign fund to the holder of the draft by virtue of the bookkeeping entries described above and that the respondent (who is not the payee or subsequent holder but is the inland bank which issued the draft) by taking up the draft became subrogated to the holder's rights. The Circuit Court found it unnecessary to determine whether the payment had been originally received by the bankrupts in a fiduciary capacity.

## III

### The Contentions of Petitioner—Trustee.

The Petitioner-Trustee contends that the bankrupts—depositors of the foreign bank—at all times remained a creditor of the foreign bank for the amount credited to the "Drafts Payable" account until the draft was presented and paid because they retained control of the amount so credited. This being so it was therefore property which passed to the Trustee under Bankruptcy Act, Section 70-a (3) (5). The bankrupts' only obliga-

tion was to "protect"* the drafts drawn by the inland bank under the drawing service, that is to say, to see to it that the draft was paid upon its presentation. There was no obligation or intention to create or irrevocably appropriate and assign a specific fund *in advance*. In essence, the obligation of the bankrupts under the drawing service was to take care of the draft of the inland bank, just as if it were its own draft. The transaction was the simple ordinary banking transaction—namely, the protection by B of the draft of A—the payment of A's draft from B's credit.

## IV.

### The Basis of the Court's Decision Contrary to the Uncontradicted Evidence as to History and Purpose of "Drafts Payable" Account.

The Court below referred to a clause in the "drawing service" contract under which the bankrupts agreed that upon their receipt of advice of the drawing of the draft and payment as aforesaid, they would "provide the drawee with funds sufficient for the payment of the draft abroad, by a transfer of credit from our balance or otherwise." It then held that the credit to the "Drafts Payable" account by the foreign bank, when it received the bankrupts' advice, was done in pursuance of the bankrupts' obligation under the foregoing quoted provision, and that it was intended to and did constitute an equitable assignment to the *holder of the draft* of the balance so credited. This conclusion was reached despite the fact that no claim is made that the holder of the draft ever had knowledge of the contract between the bankrupts and the inland bank or indeed of the existence of the bankrupts in the transaction at all, or of the credit to the "Drafts Payable" account.

*Defined in *Wabash R. R. vs. Ham*, 114 U. S., 587, 596.

The Court's conclusion also ignores the uncontradicted evidence relating to the purpose and history of the "Drafts Payable" account, and the intention underlying its use.

It appeared in evidence without contradiction* that the "Drafts Payable" account is an account which has been maintained generally by international bankers, both abroad and in this country and is maintained irrespective of any special contract for its creation. It appeared further that it is the universal custom of international bankers, upon being advised by their depositor of the drawing of a draft (either by the depositor himself or under his protection) forthwith to charge the depositor's account and to credit the amount of said draft to a "Drafts Payable" account. This is an omnibus account to which amounts of all drafts advised by all depositors are credited, irrespective of the nature of the depositor's obligation or the drawee's knowledge thereof. It appeared further that this is a practice of long standing and that there are two reasons for such practice. First, that by making such bookkeeping entries, the drawee bank at all times knows the total of the outstanding demand obligations upon it and can put itself in a position to meet the drafts which had been advised. Second, while the drawee pays interest on the depositor's general balance, it is enabled to use the fund in the "Drafts Payable" account during the period before the presentation of the draft without paying interest thereon as its sole compensation for its services in the transaction. The testimony also showed that despite the bookkeeping entries made as aforesaid, the depositor who has the account in the foreign drawee bank *can cancel the advice* of drafts drawn either by itself or under its protection without obtaining the consent of the payee of the draft or of any other person, and that the foreign

*The evidence appears in detail in the annexed brief at p. 31 hereof.

bank recognizes and obeys only the instructions of its own depositor."

To all of this uncontradicted testimony negativing an intention to treat the credit of the "Drafts Payable" account as an equitable assignment and showing that the balance in the "Draft Payable" account at all times was under the control of the bankrupts, the Court below gave no weight whatever.

## V.

### The Decision in the Zimmerman & Forshay Case.

That the credit to the "Drafts Payable" account was not made because of the special provisions of the bankrupts' drawing service but in pursuance of the independent international banking practice outlined above is emphasized by a consideration of the facts in *Matter of Zimmerman & Forshay, ex parte Henry G. Gray*, argued and decided below with the case at bar. The opinion in that case appears at p. 13 *post* as Appendix A hereof. There the bankrupts sold to Gray a draft which *they themselves* drew upon a foreign bank with which they maintained a balance. There was no special contract. The draft was advised abroad, charged to the bankrupts' account and credited to a "Drafts Payable" account in the same manner as in the case at bar. The advice was cancelled after the bankruptcy and before the draft was presented and the funds were returned to the Receiver. It appeared also in that case by stipulation that the dealings between the bankrupts and the foreign bank were such that when the bankrupts drew a draft on a foreign bank "and later for any reason wished to stop payment, that a direction to stop such payment would be honored by the bank." Despite the absence of even the semblance

"It is stipulated (fol. 378) that "This [the cancellation by the foreign bank] was done without knowledge on the part of the R. C. I. [the drawee] as to whether such draft or drafts were in the possession of the bankrupts, the drawee banks or third persons."

of a special agreement or of any agreement at all, for the creation of a fund abroad, a majority of the Circuit Court of Appeals held that the claimant was entitled to assert reclamation rights in the balance returned.

## VI.

### The Fundamental Errors of the Court Below.

The uncontradicted evidence in the present case as to the purpose and history of the "Drafts Payable" account and the fact that in the *Zimmerman* case there was no special agreement between the parties, both prove that the creation and existence of the "Drafts Payable" account in no wise was dependent upon an agreement between the American parties to the transaction. The fundamental error of the Circuit Court, therefore, lies in its conclusion that the credit to the "Drafts Payable" account was an appropriation *in advance of the presentation of the draft* pursuant to the special agreement between the bankrupts and the inland bank, whereas, as just stated, it clearly appeared:

(a) That that credit had nothing whatever to do with the special agreement; and

(b) That in cases where the bankrupts themselves were the drawers of the drafts and had made no special agreement, precisely the same practice was pursued by the drawee bank. That this is so is confirmed by the actual state of facts in the *Zimmerman* case where Zimmerman themselves drew their draft without a special agreement and the drawee bank charged the Zimmerman account and credited the "Drafts Payable", as in the case at bar.

The second underlying error is the Court's interpretation of the uncontradicted testimony as to the history and purpose of the "Drafts Payable" account, and its

failure to give effect to the fact that the foreign bank always recognized the right of the bankrupts to cancel advices prior to the presentation of the draft as is strikingly illustrated by the fact that even after bankruptcy the Receiver's directions were honored by the foreign bank. The *bankrupts* remained creditors of the foreign bank until presentation of the draft.

A third underlying error of the Court below was its conclusion that as a result of the bookkeeping entries abroad there was an equitable assignment in favor of the *payee or subsequent holder* of the draft which could be enforced against the Trustee in bankruptcy. The Court overlooked the elementary principle that an equitable assignment is not absolute but may be revoked by the assignor at any time before the assignee has been notified of the assignment and has expressly or impliedly assented thereto.* As has already been stated, there is no evidence or claim that the holder of the draft (upon which the name of the bankrupts did not appear) at any time had any knowledge of the provisions of the "drawing service", of the creation or existence of the "Drafts Payable" account, or indeed of the existence of the bankrupts themselves. This being so, it is submitted that the Court below erred in failing to hold that the foreign balance was at all times subject to the absolute and sole control of the bankrupts and that accordingly such balances passed to the Trustee under section 70 (3) and (5) of the Bankruptcy Act as "property which prior to the filing of the petition he [the bankrupt] could by any means have transferred * * *."

## VII.

### Important Reasons Why This Court Should Grant the Writ.

As already stated over two hundred and twenty in-

*See 2 Pomeroy Eq. Jur. (Fourth Ed.) Sec. 1281, post, page 42.

land banks and bankers have filed similar reclamation claims.

Your petitioner submits that the authoritative determination of the questions presented is of the greatest importance to the commercial and banking world for the reason that the banks and banking houses are daily "*protecting*" abroad drafts and checks drawn by their inland correspondents in large number and amounts and are to a similar extent drawing *their own drafts* directly upon their own foreign correspondents. Your petitioner believes that in such transactions all drafts advised to most of the European countries and drafts advised by such European countries to banks in this country are universally charged to the account of the drawer and credited to a "Drafts Payable" account when the advice is received. Your petitioner submits that neither this Court nor any other court in this country has heretofore had occasion to pass upon the effect of these bookkeeping entries nor upon the intention underlying the creation of "Drafts Payable" accounts nor upon the effect of the well established international banking custom giving to the depositor the right to control the credits in the "Drafts Payable" account. Involved in these questions is the further important question: At whose risk the fund is held abroad after the receipt of the advice by the foreign bank and the credit to the "Drafts Payable" account, in the event of the failure of the foreign bank? This case may present for determination the further important question of whether an international banker who receives funds in payment for a draft, either drawn by himself or drawn under his protection, receives such funds in a fiduciary capacity or whether his obligation is purely contractual.

## VIII.

### Conflict in Decisions.

Your petitioner submits that the decision of the Circuit Court of Appeals interpreting the bookkeeping entires and determining that the setting up of the "Drafts Payable" account was intended to constitute an equitable assignment of that balance is in direct conflict with principles underlying the decisions of the New York Court of Appeals in *Noyes* vs. *First National Bank*, 180 App. Div., 162, affirmed *on opinion below*, 224 N. Y., 542, and the very recent case of *Erb* vs. *Banco di Napoli*, 243 N. Y., 45, and in fact with the decision of the Court below in *In re Interborough Consolidated Corp.* (1923) 288 Fed., 334, certiorari denied 262 U. S., 752, all involving special accounts for the payment of coupons which accounts were there held to be general assets of the estate.

## IX.

Wherefore, because of the importance to the banking and commercial community of the question presented and because of the conflict in principle between the decisions of the Circuit Court of Appeals for the Second Circuit and the New York Court of Appeals, your petitioner respectfully prays that a writ of certiorari may be issued out and under the seal of this Court directed to the Judges of the United States Circuit Court of Appeals for the Second Circuit, demanding them to certify and send to this Court a transcript of the record of the proceedings in this case to the end that the decree of said court may be reviewed and that your petitioner may have

such other and further relief in the premises as to this court may seem appropriate.

THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in bankruptcy of Knauth, Nachod & Kuhne.

By SAMUEL ARMSTRONG,
Vice-President.

STATE OF NEW YORK, }
County of New York, } ss.:

SAMUEL ARMSTRONG being duly sworn, deposes and says that he is the Vice-President of The Equitable Trust Company of New York, the petitioner above named; that he has read the foregoing petition and knows the contents thereof and that the same is true to his own knowledge, except as to the matters therein stated to be alleged upon information and belief, and as to those matters he believes it to be true.

SAMUEL ARMSTONG.

Sworn to before me this
27 day of September, 1926.

JOHN E. McGUIRK,
Notary Public, Bronx County,
Certificate filed New York County.

CERTIFICATE OF COUNSEL.

I hereby certify that I have examined the foregoing petition and in my opinion it is well founded and the case is one in which the prayer of the petitioner should be granted by this Court.

GODFREY GOLDMARK,
Counsel.

## APPENDIX A.

### Opinion in Zimmerman Case.

UNITED STATES CIRCUIT COURT OF APPEALS,

FOR THE SECOND CIRCUIT.

*In Re*

ZIMMERMAN & FORSHAY,
Bankrupts,

*Ex parte*

HENRY G. GRAY,
Appellant,

GORDON AUCHINCLOSS, Receiver,
Appellee.

Before: Rogers, Banton and Hand, Circuit Judges.

Appeal from an order of the District Court for the Southern District of New York denying priority to the appellant's claim in bankruptcy.

The bankrupts sold to the appellant a draft drawn upon a Bohemian bank for one hundred thousand Czech crowns. On the same day they credited the drawee with the draft on their books and advised it that they had so drawn. The drawee before petition filed received the advice, charged the face of the draft against the bankrupts' balance on its books, and credited it to another account entitled "drafts payable." The draft was presented and dishonored after petition filed, and the receiver procured a reversal of the credits by the drawee and a remittance of the full balance.

WILLIAM E. SIMS and CHARLES M. KRITZMAN, for the Appellant,

WILLIAM ST. JOHN TOZER for the Appellee.

HAND, Circuit Judge: This is a companion case to In Re Gubelman, ex parte First National Bank of Trinidad, decided herewith. There are some differences in fact: the bankrupts, as drawers, remained generally liable on the draft, and had made no specific contract with the holder (or drawer), to transfer any credit on the drawee's books. Thus the case is somewhat weaker for the petitioner. Nevertheless it appears to us that the skeleton of the transaction is the same. Although it is not so proved, we think that we must assume that when on receipt of the advice the drawee made the entries upon its books, it did so in pursuance of a pre-existing agreement with the drawers. At any rate it is proved that the drawee advised the drawers of what it had done, and there is no evidence that the drawers protested.

Upon that assumption we think that the drawers' advice must be interpreted as a request to the drawee to transfer the credit in the way which it actually adopted. Moreover, when the drawers sold the draft, they promised that it should be paid on presentation (New York Negotiable Instruments Act Sec. 111). Perhaps it is conceivable that the drawee would pay the draft without being then in funds, but banking is not ordinarily done in that way, and we think that the implied agreement of the drawers was that they would, either by remittance or by a transfer of credit, cover the draft before its due date. They chose to transfer the credit and they succeeded, because the drawee had complied with their order before bankruptcy. The prior practice between the drawers and the drawee of stopping payment of such drafts is not shown to have been exercised inimically to outstanding drafts; certainly it was unlawful, if it was.

Order reversed and priority awarded.

Judge Rogers through illness was unable to take part in the decision of this case, but he had provisionally voted for affirmance.

## BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

### Detailed statement of facts showing the successive steps in the transactions between the parties.

The First National Bank of Trinidad, Colorado (hereinafter referred to as the Trinidad Bank) and numerous other inland banks and bankers maintain no foreign balances, have no foreign correspondents and have no facilities for selling drafts on foreign banks and bankers. In order to enable the inland banks to issue drafts in their own names and perhaps to impress their customers with the facilities which the banks were able to offer, K. N. & K. offered a "drawing service," under which the various inland banks could draw *their own drafts* on foreign correspondents listed by K. N. & K. just as if the inland banks did have foreign correspondents, and K. N. & K. undertook to provide for the payment of such drafts upon their presentation.

In summary, the procedure was as follows:

(1) K. N. & K. sent to their inland bank correspondents, including the Trinidad Bank, daily rate cards fixing the rate for the various foreign currencies (Italian lire in this case) under the drawing service (fols. 70, 434). The rates quoted were "good" only during the day printed on the cards (fol. 434).

(2) Upon the request of its customers in Colorado, the Trinidad Bank would sell *its own draft* on one of the foreign correspondents named in K. N. & K.'s list for the desired amount of foreign currency and would receive payment therefor at the rate fixed in the rate card, plus whatever profit the Trinidad Bank sought to

charge. *The name of K. N. & K. did not appear on the draft.* As far as the inland customer knew, the Trinidad Bank maintained direct relations with the foreign correspondent (fols. 70-72).

(3) Immediately upon the issuance of the draft, the Trinidad Bank would send an advice to K. N. & K. (Claimant's Exhibit 4, p. 161), advising of the drawing of the draft and requesting K. N. & K. "to protect same upon presentation." Remitted with the advice was a sum in American dollars at the rate fixed in the rate card.

(4) Upon receipt of the advice and check, the check was deposited in one of the general checking accounts of K. N. & K., in the Guaranty Trust Company in this case (fol. 74).

(5) Upon the day that the advice was received from the Trinidad Bank, K. N. & K. also sent its advice to the bank upon which the draft had been drawn by the Trinidad Bank, including in such advice all drafts which had been drawn that day on that foreign correspondent of K. N. & K. by all *other* inland banks availing themselves of the "drawing service" and *by K. N. & K. themselves.* All the advices to one foreign correspondent which went forward by one steamer were known as a "Steamer Block" (fol. 75).

(6) The "Steamer Block" was in two parts—(a) one advice to the main office of the foreign drawee, and (b) an individual advice to each branch of the foreign drawee upon which drafts had been drawn that day (fol. 76). The advice to the *main office* of the foreign bank upon which the draft was drawn (the Banca Commerciale Italiana in this case, hereinafter for convenience referred to as B. C. I.) requested the B. C. I. "to *protect* to the debit of our account the drafts as per particulars on

the attached copies." (Claimant's Exhibit 6, p. 163). Attached to the foregoing, were copies of the advices which had been sent to the *branches* of the B. C. I. (Claimant's Exhibits 6A, 6B, 6C, 6D, 6E). The particular draft here involved is found in the advice sent to the Sassari Branch of the B. C. I. (Exhibit 6D). This advice to the branch banks contains the following direction:

> "Please *honor* the above listed drafts charging same to *our* account with Banca Comm. Italiana Genoa."

(7) When the B. C. I. received the above mentioned advices, it thereupon debited the account which K. N. & K. maintained with the bank at its Genoa office to the extent of the aggregate of the drafts, and simultaneously credited on its books an account termed "drafts payable," in which account were also credited amounts of drafts which were advised to the B. C. I. for payment by other depositors or clients of the B. C. I. (fol. 92). Thereafter, no interest was allowed to K. N. & K. or to anyone else upon the amount credited to the account termed "drafts payable," but on the other hand, the B. C. I. received no compensation for its services in honoring drafts except the compensation measured by its use, without the payment of interest, of the money in the drafts payable account (fol. 93).

(8) *All drafts were thus dealt with whether drawn by K. N. & K. themselves or drawn by their inland correspondents* (See Claimant's Exhibit 6A).

(9) *It appears in evidence without contradiction that there is a well recognized banking custom of long standing, under which the foregoing practice is pursued, and that the reasons for the practice are that by making such bookkeeping entries (a) the drawee bank at all times knows of its possible demand obligations and can put it*

*self in a position to meet the drafts which have been advised, and (b) as sole compensation for its services in the transaction, it is enabled to use the funds during the interval before the presentment of the drafts without paying interest thereon* (fols. 93, 359).

(10) It also appears without contradiction that under the well established banking custom and practice, the American depositor who has an account in the foreign bank *may cancel the advice* of a draft *drawn either by himself or by his inland correspondent*, without obtaining the consent of the payee of the draft or the inland correspondent, and that the foreign bank recognizes and obeys only the orders of its own client without inquiring as to any one's else instructions (fols. 368, 377). K. N. & K. had regular forms for cancelling advices used for both their own and inland bank drafts (Trustee's Exhibits 3 and 4, p. 192 and fol. 383). *Thus it appears that at all times K. N. & K. kept control over their foreign balances and could cancel the advices as they saw fit.*

(11) In the present case, the advice of the Trinidad draft was not cancelled prior to the filing of the petition in bankruptcy, but immediately upon the appointment of the receiver, he cabled to the B. C. I. that he had taken possession of the assets and that all credit balances must be held subject to his order (Claimant's Exhibit 10, fol. 520). Thereafter, the balances in the general account of K. N. & K. with the B. C. I. *and the balances in the drafts payable account* were returned to the receiver by the B. C. I.

(12) *After* the bankruptcy, the draft was presented and payment refused (fol. 330).

**Holdings Below.**

The Circuit Court of Appeals held that there was an

equitable assignment in favor of the holder of the draft and that the respondent-reclaimant, having taken up the draft, was subrogated to the rights of the holder. The court found it unnecessary to determine whether or not the moneys received by the bankrupts from the Trinidad Bank were received in a fiduciary capacity, or whether, as stated in the contentions of the Trustee below, the relationship was purely contractual and the parties dealt as independent contractors.

**Brief of the Argument.**

The Trustee contends:

I.

That there was no agreement equitably to assign any funds abroad and that the acts of K. N. & K. after the receipt of the American dollars, did not constitute an equitable assignment; that these acts were done with wholly different intent and solely in pursuance of the banking practice already described.

II.

That an equitable assignment is not absolute but may be revoked by the assignor at any time before the assignee has been notified of the assignment and has expressly or impliedly assented thereto and that until such modification and assent, the foreign balance was at all times subject to the absolute and sole control of the bankrupts, and that, accordingly, such balance passed to the trustee under Section 70 (5) of the Bankruptcy Act as the "property which prior to the filing of the petition, he (the bankrupt) could by any means have transferred • • •."

III.

That under the terms of the drawing service and the forms provided therewith, no trust relationship arose between the Trinidad Bank and K. N. & K. The parties dealt as independent contractors and that the moneys paid to K. N. & K. by the Trinidad Bank were paid for K. N. & K.'s obligation to produce a certain result, namely, the honoring of the draft by B. C. I. upon its presentation. In short K. N. & K. agreed to protect, in the same manner as drafts drawn by themselves, the drafts drawn by the Trinidad or other inland banks.

## POINT I.

**Neither the contract of the parties nor any of the acts done by K. N. & K. or the B. C. I. after the receipt of the American dollars by K. N. & K. were intended to constitute or did constitute an equitable assignment of K. N. & K.'s balance in the B. C. I. as claimed by the respondent.**

Petitioner will

A. State the legal principles applicable to equitable assignments.

B. Indicate what the respondent's contentions are and what their necessary results must be.

C. Show that there was initially no intention or obligation to make an assignment—which will involve an analysis of the contract of the parties.

D. Analyze the acts of K. N. & K. and the B. C. I. after the receipt of the American Dollars by K. N. & K. and show that the acts of both of these parties were not intended to constitute an equitable assignment of any fund in pursuance of any contract, but were done merely in pursuance of well established banking practices under which the credit always remained the property of and under the control and subject to the disposition of K. N. & K. until the presentation and payment of the drafts.

**A. Tests of Equitable Assignments.**

(1) There can be no equitable assignment of a fund to come into existence unless (*a*) there was an intention to create an assignment; (*b*) such intention has been carried out and a *res* has been set up, the creation of which is carrying out of the intention. Whether or not certain acts amount to the setting up of a *res* is in turn dependent upon the intention with which those acts are done.

*Hamer* vs. *Sidway* (1891), 124 N. Y., 538.

*In re Interboro Consolidated Corporation* (C. C. A. 2nd, 1923), 288 Fed., 334-349, where this Court quotes with approval *Hopkinson* vs. *Forster*, as follows: "You can have no charge in equity without an intent to charge."

(2) There can be no equitable assignment unless the assignee consents to the setting up of the fund and agrees to look to that fund *alone* for the performance of the obligation.

*Spellman* vs. *Banker Trust Company* (C. C. A., 2nd), 1925, 6 Fed. (2nd), 799.

3 *Pomeroy Eq. Jursiprudence* (4th Ed. 1918), Section 1280, says: "The sure criterion is, whether the order of direction to the drawee, if

assented to by him, would create an absolute personal indebtedness payable by him in all events, *or whether it creates an obligation only to make payment out of the particular designated fund.*"

(3) If the fund or balance set up remains at the risk of the alleged assignor, there has been no equitable assignment.

*Tiernan* vs. *Jackson* (1831), 5 Peters 579, 594;

*Williams* vs. *Everett* (1811), 14 East, 581, 596.

*In re Interboro Consolidated Corporation*, 288 Fed., 334-345, quoting with approval Story's Commentaries on Equity, Section 1045, where it is said: "The true test whether an absolute appropriation is made out or not depends upon the point at whose risk the property is; and until the creditor has consented, the property will clearly be at the risk of the assignor or remitter."

(4) If the alleged assignor retains control over the fund or balance or may revoke his instructions with respect thereto, then there has been no equitable assignment.

In *Christmas* vs. *Russell* (1871), 14 Wall. 69, the Supreme Court said at p. 84:

"An agreement to pay out of a particular fund, however clear in its terms, is not an equitable assignment; a covenant in the most solemn form has no greater effect. * * * The assignor must not retain any control over the fund—any authority to collect, or any power of revocation. If he do, it is fatal to the claim of the assignee. The transfer must be of such a character that the fundholder can safely pay and is compellable to do so, though forbidden by the assignor."

In *Cushings* vs. *Chapman* (C. C. Mo., 1902), 115 Fed. 237, the Court said at p. 239:

> "I understand the law to be that a mere promise, however clear or solemn in character, to pay a debt out of a particular fund, does not operate as an equitable assignment of the fund, and especially so when it is a part of a mass of property to be thereafter created. To constitute such an equitable assignment, there must be such an actual or constructive appropriation of the fund or subject matter 'as to confer a complete and present right on the party meant to be provided for, although the circumstances do not admit of its immediate existence'; *that, if the holder of the fund could retain control over it, with the power, sua sponte, on his part, to satisfy the promise in cash, it is fatal to an equitable assignment. Christmas* vs. *Russell*, 14 Wall 69, 20 L. Ed. 762; *Bank* vs. *Beal* (C. C.) 54 Fed. 577; *Badgerow* vs. *Trust Co.* (C. C.) 74 Fed. 925; *Ex parte Tremont Nat. Bank*, 24 Fed. Cas. 184; *Foss* vs. *Cobler*, 105 Iowa, 731, 75 N. W. 516; *Stearns* vs. *Insurance Co.*, 124 Mass. 63, 26 Am. Rep. 617; *Williams* vs. *Ingersoll*, 89 N. Y. 518; *Hicks* vs. *Brick Co.*, 94 Va. 746, 27 S. E. 596; *Hassack* vs. *Graham*, 20 Wash. 192, 55 Pac. 36."

> See also *In re Stiger*, 202 Fed. 791 affirmed (C. C. A. 3rd, 1913), 209 Fed. 148;
> 5 *Corpus Juris*, 913.

The following acts have been held not to indicate an intention to create an assignment:

(1) The mere advice to a bank of the drawing of a draft in accordance with international banking practice does not indicate an intention equitably to assign any of the depositor's balance with the drawee.

> *Eastman Kodak Company* vs. *Park National Bank* (D. C. S. D. N. Y., 1916), 231 Fed., 320 (opinion by Learned Hand, D. J.), affirmed no opinion in this Court, 247 Fed., 1002.

(2) The mere direction to pay a draft and charge it to the account of the depositor does not constitute an equitable assignment nor is there an equitable assignment even if the funds have been placed in the hands of the depositary as a *means* of satisfying the depositor's absolute obligation.

*National City Bank* vs. *Hotchkiss* (1913) 231 U. S., 50;

*Eastman Kodak* vs. *Park National Bank* (1916), 231 Fed., 320, aff'd. 247 Fed., 1002;

3 *Pomeroy Eq. Jur.* Sec. 1282, cited with approval in the *Interboro* case, *supra*, at 345, and citing *Cheney* vs. *Libbey*, 134 U. S., 68, 83;

*Aetna National Bank* vs. *Fourth National Bank* (1871), 46 N. Y., 82, 87.

(3) Even an agreement to pay a debt out of a designated fund does not give an equitable lien on the fund or operate as an equitable assignment thereof.

*Williams* vs. *Ingersoll* (1882), 89 N. Y., 508;
*Christmas* vs. *Russell* (1871), 14 Wall, 69.

(4) Mere book entries dividing a bank balance into two or three accounts, as a matter of convenience or in pursuance of a well established custom, do not evidence an intention to assign a fund, and do not constitute an equitable assignment.

*In re Interboro Consolidated Corporation*, *supra*;

*Noyes* vs. *First National Bank* (1st Dept. 1917) 180 App. Div., 162, affirmed on opinion below, 224 N. Y., 542;

*Taussig* vs. *Carnegie Trust Co.* (1st Dept. 1913) 156 App. Div., 519, affirmed no opinion 213 N. Y., 627, and analyzed page 33, *supra;*

*Kuehne* vs. *Union Trust Company,* (1903), 133 Mich., 602, analyzed page 34, *supra.*

**B. The Necessary Results of Respondent's Contentions.**

If the respondent's contention that a fund with the B. C. I. was intended to be and was equitably assigned to it by K. N. & K. be sound, the following results would exist under the foregoing authorities:

(1) At the moment the fund was created, (if a "fund" was created) and even prior to the presentation of the inland draft, K. N. & K. was fully discharged.

(2) At the moment the fund was set up, K. N. & K. lost all control over it and the debtor-creditor relationship between B. C. I. and K. N. & K. ceased.

(3) After the fund was set up, it was wholly at the risk of the inland bank; that is, if the B. C. I. in the present case, or if in other cases any one of the hundreds of scattered correspondents named in the list, became insolvent after the fund was set up and before the draft was presented, or for any reason failed or refused to pay the draft upon presentation, the loss would fall, not on K. N. & K., but on the inland banks.

(4) The various steps taken by K. N. & K. would have to be construed as necessarily taken to carry out their previous intention and promise as found in the provisions of the drawing service to create and assign a fund abroad, *despite the fact* (*a*) that no such construction is made when those very same steps are taken in those cases where K. N. & K. issue their own drafts without any such previous promise, and (*b*) that such

steps are taken by international bankers generally in pursuance of well established usage and custom existing for wholly different reasons and irrespective of any special promise.

It will now be shown however, that no such results were intended or effectuated; that K. N. & K. were not discharged until payment of the draft; that K. N. & K. at all times controlled the funds on deposit with B. C. I.; that the risk of loss in the event of the failure of B. C. I. was on K. N. & K. and not on Trinidad; and, finally, that the very steps here taken were the usual and ordinary steps taken in accordance with general international practice and custom, and, indeed, the same steps taken by K. N. & K. in protecting drafts drawn by themselves although no agreement in the nature of the drawing service was entered into with respect to such drafts.

As a result, there is no basis for respondent's contention that funds were equitably assigned in favor of Trinidad or the payee of the draft.

**C. Neither the Provisions of the Drawing Service nor the Acts Done in the Performance of K., N. and K's. Obligations were Intended to or Did Constitute an Equitable Assignment.**

Having now stated the basic legal principles involved and the necessary results of respondent's contentions, the *contract* of the parties and the *acts* done pursuant thereto will be examined and it will be shown that there was no equitable assignment.

> 1. The provisions of the drawing service and the forms provided for use therewith, do not disclose any intention that any fund should be created or assigned for the payment of the draft drawn by Trinidad on the B. C. I.

An examination of the drawing service and the forms

supplied in connection therewith shows that K. N. & K. was under an absolute contractual obligation to see to it that the draft was paid upon presentation and that they could not be discharged until such payment was accomplished; that is the end which Trinidad desired. It had drawn a draft upon a bank which it did not know—it relied solely upon K. N. & K. and their facilities. Accordingly, K. N. & K. undertook that upon receipt of the advice of the drawing of the draft by Trinidad and the receipt of the consideration in American dollars:

> "We shall promptly forward our advice of the same and provide the drawee with funds sufficient for the payment of the draft abroad by a transfer of credit from our balance, or otherwise" (fol. 422).

What this meant, of course, was that K. N. & K. undertook to notify the foreign bank that the draft had been drawn, and further undertook to see to it that the foreign bank would pay the draft when it was presented. Such payment was to be accomplished by *means* of a transfer from K. N. & K.'s balance, that is, by a debit to the K. N. & K. account, or was to be accomplished "otherwise," which, of course, meant that in those cases where K. N. & K. had no foreign balance in the particular bank, provision would somehow be made by K. N. & K. for having the draft paid—for example by directing a foreign bank with which they did have a balance to arrange for the payment of the draft when presented to the drawee, i. e., to "protect" the draft.

That nothing more than this was intended and that K. N. & K.'s obligation was an absolute and personal one, and not one dischargeable by the creation of a fund, would further appear from the forms, provided with the drawing service, particularly the advice from Trinidad to K. N. & K. that the draft had been drawn (Claimant's Ex. 4, fol. 482). This advice states that Trinidad has

sold the draft in pursuance of the drawing service and states that Trinidad:

> "shall thank you to *protect* same upon presentation."

This direction certainly negatives any idea that K. N. & K. was to discharge their obligation by the creation of a fund.

The phrase "to protect a draft upon presentation" has a well recognized meaning. Such an undertaking is one to see to it that the draft is *paid*. This appears clearly from the case of *Wabash Railroad Co.* vs. *Ham*, 114 U. S., 587, 596. That this was the meaning understood by K. N. & K. is confirmed by the language of the advices which K. N. & K. sent to the B. C. I. (Claimant's Exhibit 6 and 6D). These advices are a clear recognition by K. N. & K. that their obligation was to have the draft honored at presentation to the debit of their account. If the intention had been that K. N. & K. should assign a fund for the payment of the draft in advance of its presentation, then it would have been very easy to provide simply that K. N. & K. should *set up a credit for Trinidad*, so that when the draft was presented Trinidad would have a credit on the B. C. I. books to which the draft could be charged. This is accomplished daily by the ordinary cable or mail transfer. If this had been the intention, the lengthy instructions and provisions of the drawing service would have been unnecessary. But this was not at all the intention of the parties or the scheme of the drawee service. The underlying intention of the service was that the draft should be treated just like a draft K. N. & K. itself had drawn; and just as K. N. & K. would direct the B. C. I. to pay their own drafts, and would, of course, have a balance there at the time of presentation to meet them, so the scheme was to protect the payment of the inland draft by having a balance with the B. C. I. at presentation for its payment, charging it

to the K. N. & K. account. The balance in the form of K. N. & K. credit had to be there at the moment of presentation and not before.

That this was what the parties had in mind is further evidenced by the preliminary statement in the List of Foreign Correspondents (Claimant's Exhibit 1, fol. 418), for there the opening paragraph states that:

> "Inasmuch as the mantenance of a Foreign Department *involving the carrying of balances abroad*, etc., is undesirable from the standpoint of a majority of the inland banks, we have aimed for many years to supply this want by *extending* to our correspondents the privilege of using *our* world-wide facilities for carrying on a foreign exchange business."

It was thus the basic purpose of the drawing service to substitute K. N. & K.'s foreign credit for the necessity of the inland banks having balances abroad; for that was declared to be "undesirable."

Of course, *extending* to the inland correspondents the privilege of using the world-wide facilities *of K. N. & K.* for carrying on a foreign exchange business simply meant that K. N. & K. would make available for the payment of the inland bank drafts *K. N. & K.'s* own balances or credit in foreign countries which K. N. & K. would direct to be charged upon the honoring of the draft (Claimant's Exhibit 6D, fol. 499), when presented. *The scheme here devised was, in its essence, a mere substitute for the purchase by the inland bank of K. N. & K.'s own drafts upon which K. N. & K. would remain liable* despite the *failure of the foreign correspondent.*

It is apparent, therefore, that under the drawing service and the forms used, which together evidence the contract of the parties, there was no intention that any fund should be assigned or appropriated to the payment of the draft. The absence of any such intention *is of*

*itself fatal* to the contention now advanced (to obtain a preference over other creditors) that any of the balances of K. N. & K. at the time of the filing of the petition in bankruptcy had been equitably assigned.

> 2. The acts done by K. N. & K. and by the B. C. I. in the performance of K. N. & K.'s obligation under the drawing service, including the bookkeeping entries made by the B. C. I. pursuant to a well established international banking custom, are no evidence of an intention to assign or appropriate a fund. This is particularly so, inasmuch as K. N. & K. at all times retained control of their balance and had the right to cancel advices, and thus remained the creditor of B. C. I.

It has just been shown that the contract of the parties did not contemplate an assignment or appropriation of a specific fund abroad. It will now be shown that the *acts* of the parties do not evidence an equitable assignment.

On receipt of the Trinidad bank's check in American dollars (Claimant's Exhibit 3, fol. 481) together with the advice from Trinidad (Claimant's Exhibit 4, fol. 482) K. N. & K. promptly sent an advice to the B. C. I., upon which Trinidad had drawn its draft. Such advice was composed of a statement to the main branch of the B. C. I. at Genoa (Claimant's Exhibit 6, fol. 487) containing a statement of all drafts drawn on the B. C. I. and its branches for a given period and instructing the B. C. I. to "please protect to the debit of our account the drafts as per particulars on the attached copies." The "attached copies" were copies of advices which Knauth, Nachod & Kuhne had sent to each of the individual branches of the B. C. I. upon which drafts had been drawn by them or under their protection (see Claimant's Exhibits 6A-6E, fol. 490, *et seq*). One of such copies (Claimant's Exhibit 6D, fol. 499) was addressed to the Sassari branch of the B. C. I. and included an ad-

vice of the draft here in question drawn by the Trinidad Bank. Such advice reqested the B. C. I. to "please honor the above listed drafts charging same to our account with Banca Comm. Italiana, Genoa."

It is important to note that included in the advice sent to the B. C. I. by K. N. & K., were drafts drawn not only by inland bank correspondents of K. N. & K. (such as Trinidad Bank in this case), but also by "ourselves"—K. N. & K. (See for example, Claimant's Exhibits 6A, fol. 490 aand 6E, fol. 502). *In other words, K. N. & K. took exactly the same steps to protect the drafts drawn by themselves as were taken to protect drafts drawn by their inland correspondents under the drawing service.* It will also be shown that the B. C. I. on receipt of K. N. & K.'s advice acted in the same manner with respect to own drafts and the inland bank drafts. Therefore irrespective of other arguments, if no equitable assignment was contemplated or effected as a result of the issuance of K. N. & K.'s own drafts, none was contemplated or effected as a result of the issuance of the inland bank's drafts including the Trinidad Bank draft in this case.

**The Debiting by B. C. I.**

Upon the receipt of the advice, the B. C. I. charged the amount of all the drafts, both those issued by various inland banks and those issued by K. N. & K. themselves, to the account which K. N. & K. maintained with the Italian Bank, and

> "simultaneously credited on its books an account termed 'drafts payable' in which account were also credited amounts of drafts advised to the said Banca Commerciale Italiana for payment by other depositors or clients of the Banca Commerciale Italiana in addition to the bankrupts" (fol. 92).

The following facts are to be noted:

(1) That K. N. & K. gave no directions to the B. C. I., to set up a fund which should be irrevocably appropriated to the payment of its own and of the inland drafts, but simply directed them to protect the drafts to the debit of their account and to honor the drafts, charging the same to their account.

2. That while K. N. & K.'s account in the B. C. I. was debited with the aggregate of all the drafts, (*a*) no direction was given to set up the account in favor of the Trinidad Bank, which of course, is what ordinarily is done when a credit is established in favor of somebody by a cable transmission or otherwise; and (*b*) no account was ever set up in favor of the Trinidad Bank.

3. On the contrary all the drafts drawn by all of the depositors of B. C. I. were credited in an omnibus draft payable account, and, as will be shown, the credit in the drafts payable account "is entered in a folio under the name of the bank whose account has been charged" (fol. 350).

Yet, it is from these very acts and circumstances that the respondent urges there must be found an intention equitably to assign a specific fund for the payment of the specific drafts drawn by Trinidad.

Not only is no such intention found by the mere acts themselves, *but on the contrary*, the record shows affirmatively and without contradiction that the entries were made in accordance with well recognized international banking practices and with wholly different intention. The reasons for the existence of the international banking custom, as appears from the testimony of the witness Dawson about to be analyzed are two-fold:

(*a*) That it was a convenient method of indicating to the drawee banker what his commitments were likely

to be in the immediate future and thus enabling him to have liquid and available for immediate use enough capital to meet those commitments;

(*b*) That while the banker paid interest to his depositor on the amount standing to the latter's credit, no interest was paid on the amount of his funds credited to the Unpaid Draft Account and that the use of this latter balance between the time of its credit to the Unpaid Draft Account and the presentment of the draft drawn by the depositor or under his protection without the payment of interest thereon constituted the bank's compensation for its services in meeting the draft.

**Testimony of Dawson as to Reasons for Existence of "Drafts Payable Account."**

Ralph Dawson, Vice-President of the Guaranty Trust Company, has had extensive experience in international banking for over 25 years (fol. 345), and has had experience in all branches of foreign exchange business (fol. 340 *et seq.*) He has handled foreign exchange transactions, both where the New York banks drew their own drafts upon foreign correspondents (fol. 345) and also is familiar with and has handled transactions involving the "protection of drafts by New York banks, bankers or trust companies on behalf of inland banks" (fol. 346).

At fol. 350 he testified:

> "The Witness.—The practice is to charge the current account of the client with the sum of money and carry it over into another account which is known on the ledgers of most banks as "unpresented drafts drawn," *where it is entered in a folio under the name of the bank whose account has been charged.*"

In other words, although B. C. I. debited K. N. & K.'s general account and credited the unpresented drafts pay-

able account, the credit was entered in a folio, *not* under the name of the Trinidad Bank or the payee, *but under the name of K. N. & K.*, thereby indicating that the balance still belonged to K. N. & K.

And at fol. 350 he was asked this question:

> "Q. Is there also a general practice or custom with respect to the cancellation of advices after their receipt by the foreign bank and prior to the presentation of the draft for payment?"

And at fol. 352, he answered that inquiry as follows:—

> "A. A communication of the fact of cancellation by any means he can avail himself of, cable, letter or anything else. Upon receipt by the drawee bank that such draft has been cancelled, a reversal entry is passed, taking the amount of such cancelled draft from the unpresented draft ledger and crediting it back into the current account."

He was then asked these questions and gave these answers (fol. 353):

> "Q. And does that same custom prevail in the case of drafts drawn by inland banks, where the advice is by the New York bank? * * * A. Yes. * * *
>
> Q. Is such cancellation ordinarily and customarily effected without assigning any reason? * * * A. The drawee bank acts entirely on the orders of its client.
>
> Q. Which is the bank— A. Which is the bank that has the account on its books."

Mr. Dawson made it entirely clear that the same custom obtained in international banking, whether the New York bank had advised its own draft, or the draft of an inland bank, for he testified at fol. 368:

> "Q. You made an answer to Mr. Goldmark to the effect that these cancellations were effected

upon notification from the drawer, didn't you? A. No, sir, from the client.

Q. Then I may have misunderstood you. A. When the question was asked there was no question of a third party.

Q. You mean the person who drew the draft, when you say client? A. No, sir, I mean the name that is on the books of the drawee bank is the client or the owner of the funds.

By Mr. Goldmark:

Q. You mean the person who has the account in the bank? A. Yes, sir.

Q. They cancel the advice at his request whether he is the drawer of the draft or whether he is the person who advised the draft drawn by somebody else? A. Yes, sir, at his order they will cancel the draft."

The reasons for the existence of this custom at the present time were stated by Mr. Dawson to be as follows (fol. 357):

"Q. How has that practice developed in modern times? A. Well, the practice has hung on in modern times, like a great many other practices, and has been availed of as a means frequently of compensating a banker for an account that would otherwise be troublesome and a loss. You have many accounts frequently that are active, which on bare balances in current accounts, are a lot of trouble, and a loss in handling that would not be worth while, but there is always a non-interest bearing float that compensates you for the trouble you take.

Q. So that in reality there are two reasons, are there not, generally assigned, namely, to put the drawee bank or banker in a position to meet the drafts which have been advised, and to enable him to use that fund as he may without paying interest thereon to the person who has the account? A. That is right."

And at fol. 370:

"Q. That is, knowing how much the advised drafts are, you know how much money you have to keep as ready cash? A. Yes.

Q. And you determine the amount of drafts which are to come from your general omnibus drafts payable account? A. Yes.

Q. That is, any day, looking at your drafts payable account, you know how many outstanding advised drafts there are, how much that amounts to, and therefore, you know how much available cash you have to have in order to meet that draft? A. Yes."

And at fol. 373:

"The Master.—And under the present system does the bank have the use of that money until the draft is presented for payment?

The Witness.—Yes.

By Mr. Goldmark:

Q. They can lend it on the street? A. Yes.

Q. That is, they could lend a sum equivalent to some one on the street, so that, at any moment, if the number of drafts which had been advised, which came in on a particular day, was more than the average number that came in on another day, you would always know at the beginning of the day how much money you needed from your drafts payable account to meet outstanding drafts? A. Yes."

In addition to explaining the present practices and the reasons underlying them, Mr. Dawson testified as to the origin of these practices. He stated, in substance, that in the past when there were no Federal reserve banks, banks of rediscount or methods of suddenly raising cash, an international banker on being advised that his depositors had drawn drafts on him, would convert some of *his own* non-liquid assets into cash and hold the cash ready to meet the obligation, namely, the payment of the drafts which his depositor had drawn. He even went

so far in ancient times, Mr. Dawson believes, as to set aside his own cash in separate bags to meet separate drafts, the drawing of which had been advised. The repondent apparently seeks to attach much weight to this belief of Mr. Dawson as to the historical origin of the present custom and seeks to find therein conclusive proof of an intention equitably to assign a particular fund for the payment of a draft not yet presented.

Of course, the fallacy of the respondent's contention is obvious and is this:

The bankers in early days who are said to have set aside cash to meet advised drafts were not setting aside cash which belonged to their depositors, but *their own cash*, so that *they* would be in "possession of funds to meet their commitments" (fol. 356).

The depositor who was the drawer of the draft and the creditors of the bankers did not set aside any moneys which belonged to him. He had no intention of appropriating any specific fund to the payment of his advised draft. All he desired was that the draft should be paid upon its presentment. Of course, he had no objection or right to object if the banker in those days saw fit to liquidate his own securities in order to provide *himself* with the cash to meet the obligation. But the controlling fact is that the depositor, the drawer of the draft, always had the right to cancel the advice and therefore his acquiescence in the banker's setting aside his, the banker's own money, in no wise affected the rights of the depositor or irrevocably appropriated the depositor's money. The depositor remained the creditor of the banker until the draft was paid.

Accordingly, it is impossible, even out of this ancient practice, to spell out an intention on the part of the depositor equitably to assign or appropriate any money for the payment of the advised drafts.

As will be shown, the reservation of the right of can

cellation and the maintenance of control over the debt from the bankers to the depositor is fatal to any theory of equitable assignment.

Certainly the uniform modern practice is no more than a banking convenience, which has grown up for the reasons so clearly stated by Mr. Dawson.

As testified by Mr. Dawson, who was familiar with and had done the same kind of business (fol. 346), the practice exists with respect to all advised drafts, whether they are drawn by the American depositor himself or drawn by an inland bank under protection of the American depositor. Certainly, in the light of this well recognized banking practice, it is impossible to urge that K. N. & K. by approving of the debit thereby intended equitably to assign a part of their foreign balance. How common the practice was to cancel any and all drafts without knowledge or consent of the inland bank appears from the fact that K. N. & K. had printed forms which they used to accomplish this result (Trustee's Exhibit 3 and 4, p. 192).

The direction contained in Trustee's Exhibit 3 to cancel an advice was given without the consent of the inland bank or of the payee of the draft, even when it was not known in whose possession the draft was. Such direction was honored by the B. C. I. because at all times the B. C. I. considered itself obligated only to K. N. & K. and recognized no obligation either to Trinidad or to the payee. The reason for this was clearly stated by Mr. Dawson in his testimony at fol. 368, already quoted, where he says that the bank only recognizes the instructions of its own depositor, whether that is the drawer of the draft or whether it is the person who advised the draft drawn by somebody else.

**Other Evidence Confirming Dawson's Testimony as to Custom.**

The existence of the international banking practice to which Mr. Dawson testified is also confirmed by the testimony of Mr. Schulze (fol. 327). On this phase of the question it is important also to note Mr. Schulze's testimony (fols. 400 to 402), that in cases where dollar drafts were drawn on the B. C. I. (as distinguished from drafts drawn in lire as in the case at bar), the amount thereof was not charged against K. N. & K.'s general account on receipt of the advice and was not credited to the Drafts Payable Account, and that, therefore, inasmuch as the B. C. I. had the use of no credit without the payment of interest pending the presentation of the draft, it received a commission for honoring these dollar drafts. The application of the general custom testified to by Mr. Dawson, under which the B. C. I. looked only to its customer, K. N. & K., for instructions as to cancellation and recognized K. N. & K.'s sole control over their balances both in their general account and in the Drafts Payable account, is confirmed by the testimony of Mr. Schulze (fols. 216-219 and 234-238). The absolute control of K. N. & K. over their balance with the B. C. I. has been clearly demonstrated.

Mr. Dawson's testimony is also supported by the facts *stipulated* at fol. 378 to the effect that the B. C. I. cancelled drafts drawn either by K. N. & K. or under their protection and that

> "This was done without knowledge on the part of the B. C. I. as to whether such draft or drafts were in the possession of the bankrupts, the drawer banks or third persons."

**D. The Conclusions from the Foregoing Facts Show that the Tests of the Existence of Equitable Assignment Have Not Been Met.**

The foregoing facts establish the following propositions:

(1) There was no intention on the part of K. N. & K. or the Trinidad Bank to assign any funds abroad, K. N. & K.'s sole obligation being to have the draft paid at presentment, as in the case of drafts drawn by K. N. & K. themselves and thus see to it that Trinidad's obligation to its customer and the payee was performed. K. N. & K. agreed to furnish sufficient funds as a *means* of enabling them to perform their obligation.

(2) K. N. & K. did not direct B. C. I. to set up any particular fund but simply directed the debiting of the drafts to their general account upon presentation. And no fund was in fact set up in favor of Trinidad or irrevocably appropriated abroad. The credit to the omnibus "drafts payable" account was made, not in pursuance of K. N. & K.'s obligation under the drawing service, but pursuant to the well established international banking custom. The same practice was pursued with respect to drafts drawn by K. N. & K. themselves, although their issuance was not governed by the terms and conditions of the drawing service. This custom exists for reasons entirely independent of a desire irrevocably to create a fund.

(3) The Trinidad Bank did not agree to look to the fund abroad for the payment of the draft drawn by it, but desired and procured K. N. & K.'s general obligation "to protect" that draft when presented. *Does the respondent seriously argue that the intention underlying the drawing service as agreed to by the parties was that the large and small banks scattered throughout this country who*

*had no knowledge of foreign banks and bankers, were paying over their money to K. N. & K., relying on the credit, solvency and responsibility of foreign correspondents in scattered communities throughout Europe, wholly unknown to them and chosen by K. N. & K.?* What the inland banks wanted was that their drafts drawn upon foreign bankers with whom they had no relations whatever and of whom they knew nothing, be honored. They did not want funds set up in innumerable places throughout Europe which would be there at their risk, awaiting the presentation of the drafts. If the reverse were true, every bank throughout the country which availed itself of the service of K. N. & K. or other New York bankers, affording a like service, would have to look solely to the foreign bank, and in the event of its failure or refusal to pay, loss would not fall on K. N. & K., but on the inland banks.

(4) The balance with the B. C. I. was at all times at the risk of K. N. & K., inasmuch as they had assumed an absolute obligation to have the drafts paid on presentment, from which obligation they would not have been relived by the failure of the B. C. I., with the consequent loss of the balance.

(5) It appears from undisputed testimony of Mr. Dawson and Mr. Schulze and from the stipulations in the record (fol. 378) just referred to that both that portion of the balance standing to K. N. & K.'s credit on the books of B. C. I. and that portion credited in the drafts payable account, was at all times at the absolute control and disposition of K. N. & K. and that the B. C. I. looked only to K. N. & K. for instructions as to the disposition of both balances. That is, K. N. & K. always remained the creditor of B. C. I.

## POINT II.

**Because of the International Banking Practice and because the holder of the draft (to whose rights the Court below held the respondent subrogated) had no notice of the alleged assignment and did not consent thereto, any alleged assignment was revocable and the balance assigned remained subject to the bankrupt's control, and, accordingly was property which passed to the trustee under Section 70a (3) and (5) of the Bankruptcy Act.**

In 3 *Pomeroy Eq. Jur.* (4th Ed.), Sec. 1281, the learned author says:

> "*Notice to the Creditor-Assignee Essential.* Although, whenever a debtor, in the manner above described, makes to his creditor an equitable assignment of a specific fund or debt in the hands of or owing by a third person, the assent of such third person is not requisite to the effect of the transfer in equity, yet the assignment, appropriation, direction, or order is not absolute, but may be revoked by the debtor-assignor at any time before the creditor-assignee has been notified of it, and has expressly or impliedly assented thereto. In such a case notice to and assent by the creditor-assignee are essential to an absolute assignment."

This statement of the law is supported by numerous authorities, which it is unnecessary to consider in detail at this time.

As the bankrupts, both for the foregoing reason and because of the international banking practice already discussed, kept control of the fund, the balance credited to the drafts payable account passed to the Trustee in

bankruptcy under the following provisions of Section 70 of the Bankruptcy Act:

> "(a) The trustee of the estate of a bankrupt, upon his appointment and qualification, and his successor or successors, if he shall have one or more, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of the bankrupt, as of the date he was adjudged a bankrupt * * * to all * * * (3) powers which he might have exercised for his own benefit, but not those which he might have exercised for some other person; * * * (5) property which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him * * *."

## POINT III.

**There initially was no trust relationship and the parties dealt as independent contractors.**

In view of the fact that the Circuit Court of Appeals has found it unnecessary to pass upon this extremely important question, it will not be discussed at length at this time. In support, however, of the contention that there initially was no trust and that the parties were merely dealing as independent contractors, petitioner begs leave to refer to the following authorities:

That there was initially no trust relationship:

*Legniti* vs. *Mechanics & Metals N. B.* (1921) 230 N. Y., 415;

*Beecher* vs. *Cosmopolitan Trust Co.* (1921) 239 Mass., 48;

*Gravenhorst* vs. *Zimmerman & Forshay* (1923) 236 N. Y., 22;
*Samuels* vs. *E. F. Drew & Co., Inc.* (C. C. A. 2nd, 1924) 296 Fed., 882.

That the parties dealt as independent contractors and not as principal and agent:

*Casement* vs. *Brown* (1893) 148 U. S., 615;
*Sloan Shipyards Corporation* vs. *Fleet Corporation* (1922) 258 U. S., 549.

## POINT IV.

**The petition for a writ of certiorari should be granted.**

Respectfully submitted,

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FILED
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# Supreme Court of the United States

OCTOBER TERM, 1927.
No. 130.

THE EQUITABLE TRUST COMPANY OF NEW YORK as Trustee in Bankruptcy of KNAUTH, NACHOD & KUHNE,
*Petitioner,*

*against*

THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO,
*Respondent.*

# REPLY BRIEF FOR PETITIONER

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Of Counsel.

# Supreme Court of the United States.

OCTOBER TERM—1927.

| | |
|---|---|
| THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy of Knauth, Nachod & Kuhne, Petitioner, *against* THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO, Respondent. | No. 130. |

## REPLY BRIEF FOR PETITIONER.

### I.

### As to the Alleged Equitable Assignment.

As the result of 52 pages of argument on this point, the respondent contends that although the holder of the draft never knew of the existence of the drawing service, of K. N. & K.'s relation to the transaction, or of the Drafts Payable Account, nevertheless:

(1) By the advice from K. N. & K. to the B. C. I., followed by the debiting of K. N. & K.'s account and the crediting of the Drafts Payable Account, there resulted an equitable assignment of B. C. I.'s debt to K. N. & K. for the benefit of the holder of the draft. Respondent says at page 52:

> "Claimant has always claimed in the clearest terms and still claims that the assignment was an assignment *for the benefit of the holder of the draft, whoever he might be.*"

That statement is only confirmatory of the position now taken clearly by the respondent for the first time throughout its entire brief.

(2) That because the respondent as the drawer thereof has taken up the draft, respondent is subrogated to the rights of the holder. Respondent quotes with approval portions from the opinion in the *Mur'can* case, 13 Fed. (2d) 730, 732, decided at the same time as the case at bar, where the Court below said in distinguishing that case from this:

> "In Re Gubelman, Ex parte First National Bank of Trinidad, 13 Fed. (2d) 732, handed down today, we decided the drawer, having taken up a draft drawn under the same 'service contract', stood in the position of an equitable assignee. *It is true that this depended upon the drawer's subrogation to the holder's right, but the facts were not the same as here.*"

The errors in this argument, now so confidently advanced, are:

(A) That the law is elementary that there is no equitable assignment, and that there is in fact only a mere direction which is revocable, until the third party is notified of the supposed assignment either by the assignor or by the debtor (here the B. C. I.) and assents thereto, with the result that the risk of loss is thereafter on the third party;

(B) That even if there were an equitable assignment in favor of the draft holder, the Trinidad Bank has not been subrogated to the rights of the holder of the draft.

A.

In the absence of a notification and assent by the third party, there is no privity between the debtor and the third party. No *res* has been irrevocably appropriated and the instructions given to the debtor may be cancelled. In fact, the debtor, if he pays after such cancellation, would be liable to his creditor.

As pointed out in petitioner's main brief, the *power* to revoke—the *power* to transfer—is enough to pass title to the Trustee in Bankruptcy. The rule, as above stated, is well settled both in England and in this country; it is even recognized by counsel for the Fidelity Trust Company in its brief (p. 9) filed as *amicus curiae* herein. The reason for the rule is obvious. As pointed out by Judge Story in his *Commentaries on Equity*, Section 1045, and by Lord Ellenborough in *Williams* vs. *Everett*, 14 East 581, 596, the test of whether there is an equitable assignment depends upon the point at whose risk the so-called fund or *res* remains—who must stand the loss if the fund is lost. This being so, of course, that loss cannot be placed on the third party unless he has expressly, or impliedly at least, agreed to look to that fund or *res* as the sole source of his payment.

In England the Courts have gone far in denying to the holders of acceptances any rights against bankers to whom cash or bills were sent for collection to be used to take up the acceptances where the holders have not received notice that the cash or proceeds of bills are intended to constitute the source of the payment of the acceptances, and the holders have not consented to that arrangement.

*Grant, Bankers & Banking Companies*, page 258 (6th Edition, London 1910), in discussing special remittances to cover specific acceptances, states:

> "Rights of third parties. Where money has been paid to a banker by his customer for the purpose of taking up the particular bill, the question often arises whether the holder can claim to have the money applied in discharge of the bill. The answer depends upon whether any privity has been established between the banker and the holder of the bill. If none has been established, no action will lie against the banker either at law or in equity. *The mere fact of receiving money with oral or written directions to apply it in a particular manner will not bind the banker to third parties.* And where bankers having received money for the purpose of taking up a bill attended on the holder's agent for this purpose after the bill has been sent back as dishonored, they were not bound on the bill being subsequently presented to apply the remittance in payment of the bill. *The circumstance that the banker has appropriated the money in his books to payment of the bill is not sufficient to create privity between him and third parties.*"

*Hart's, Law of Banking*, 3rd Edition (1914) page 456, thus states the same principle:

> "But nothing short of an agreement on the part of the banker to hold funds to the use of the payee, *communicated to the latter*, will render the banker liable to him. The receipt of specific funds by bill or otherwise from his customer, with express directions to apply such funds in meeting a particular draft, will be insufficient for this purpose, even although the customer has himself communicated to the holder the instructions given to the banker, and the banker has also in guarded language, and avoiding an undertaking to pay, informed the payee of the instructions which he has received."

The law on this point was summarized, as far back as 1811, by Lord Ellenborough in *Williams* vs. *Everett*, 14 East. 581, where he said.

> "It is entire to the remitter to give, and countermand, his own directions respecting the bill as often as he pleases, and the persons to whom the bill is remitted may still hold the bill till received, and its amount when received, for the use of the remitter himself, *until by some engagement entered into by themselves with the person who is the object to of the remittance*, they have precluded themselves from so doing, and have appropriated the remittance to the use of such person."

The American authorities are to the same effect:

> 3 *Pomeroy, Equity Jurisprudence*, Section 1281 (4th Edition) quoted at page 16 of petitioner's principal brief;
> *Story, Commentaries on Equity*, Section 1045;
> 1 *Williston on Contracts*, Section 436.

The respondent recognized that notice to the assignee is a *sine qua non* of the assignment, by italicizing its statement of the additional facts which would have turned the situation in the *Interborough* case into one resulting in an assignment, for at page 34 of its brief, it says:

> "The court expressly recognized that if the creditor *were told of the setting apart and assented thereto*, a different situation would arise • • •."

In the light of these authorities, it is evident that the holder of the drafts who never knew that K. N. & K. was in the transaction, never knew of the "drawing service" and never knew of the Drafts Payable Account, could not have become an equitable assignee of the indebtedness of B. C. I. to K. N. & K. and could not have assented to look "to that fund" as the sole source of

the payment of the draft. Therefore, as there was no equitable assignment, the mere instructions given by K. N. & K. to B. C. I. were revocable—K. N. & K. at all times retained the power to transfer B. C. I.'s indebtedness to them and that indebtedness accordingly passed to the Trustee in Bankruptcy.

The error of the court below in deciding that the holder of the draft was an equitable assignee was emphasized in the *Zimmerman & Forshay* case decided on the same day where a like conclusion was reached even in the absence of a drawing service contract and as a result of the drawing of a draft by the bankrupts themselves. Clearly the court below overlooked the foregoing elementary principles.

B.

Even if on any conceivable theory the holder of the draft became an equitable assignee, it has not been explained how the respondent acquired the holder's rights, by subrogation or otherwise.

The Circuit Court of Appeals, in the *Munteau* case, expressly stated that the respondent's rights in the present case rest upon subrogation to the rights of the holder. But the opinion does not explain how the doctrine of subrogation is applicable to the present facts. If there were an equitable assignment with the result that "the fund" abroad belonged to the draft-holder, then his remedy was against the B. C. I. and the respondent as the drawer was not in default and was under no obligation to take up the draft. If this is so, the taking up of the draft by respondent was a mere voluntary act on its part which would gave it no right to subrogation. No citation of authority is needed for the proposition that unless there is a duty to pay, there can be no subrogation.

**The Bankrupts' Right to Cancel and the Payment of the Balance by the B. C. I. to the Trustee in Bankruptcy.**

Since the respondent here by its own argument has simply acquired the rights of the draft-holder and it has been shown that there was no *res* irrevocably appropriated for the benefit of the draft-holder, it follows that, even assuming the subrogation claimed by the respondent, no *res* came into the possession of the Trustee in Bankruptcy charged with the payment of the draft. Just because the B. C. I. had never notified the draft-holder of the existence of the Drafts Payable Account, and because the draft-holder had never expressly or impliedly agreed that the risk of loss of the fund was on the holder, and just because the B. C. I. recognized that until such notification and acquiescence the fund, to wit, B. C. I.'s indebtedness to K. N. & K., still belonged to K. N. & K. and was at its risk, *the B. C. I., despite the bankruptcy, recognized its obligation to pay its indebtedness to K. N. & K. and to no one else.* And, of course, the foreign bank in the *Zimmerman & Forshay* case evidently made payment to the Trustee in Bankruptcy in that case for like reason.

But, here, the petitioner need not rely on the mere negative argument that the holder never consented to the "assignment". For not only was there no notification to the draft-holder or consent by him, but in addition, *the uncontradicted testimony is that a custom existed by which the bank which advised the protected draft retained the right to cancel such advice.* In all probability this very custom grew out of the fact that until the draft-holder was notified, the right of cancellation existed.

Respondent points out that according to the record the bankrupts *had* never cancelled an advised draft ex-

cept at the request of the bank drawing the draft, and the respondent would argue from this fact that the bankrupts only had the *right* to cancel when they had been so requested. As a matter of pure reason, respondent's argument can be disposed of by pointing out that in the absence of insolvency, the bankrupts would never have had occasion to cancel a draft once advised by them, unless the drawer bank requested the cancellation. The bankrupts before advising a draft had received payment for their services in American dollars. Having received this payment, they would never desire to cancel the draft abroad except when they intended to return the American dollars paid here by the drawer. Had the bankrupts prior to the bankruptcy cancelled an advised draft without the request of the drawer, they would have been bound to repay the dollar consideration received. As a matter of law, respondent's argument may be disposed of by pointing out that the mere fact that the bankrupts never *did* cancel without having received the request of the drawer to do so, has no bearing whatever upon their *power* to do so, thus enabling them to use once more their balance abroad, leaving the drawer bank only with a general claim against the bankrupts for the amount of the consideration originally paid for the protection of the draft. This claim, in the absence of insolvency, the bankrupts would, of course, have paid out of their general funds and not out of any specific fund.

A similar argument was recently advanced to this Court by the respondent in the case of *Equitable Trust Company* vs. *Rochling*, decided November 21, 1927, where it was argued that because the respondent there *never drew* against a balance with its banker until the checks deposited to its credit had been collected, it did not have the *right* to do so. The argument was ignored by this Court which evidently held that the right existed, despite the respondent's failure to exercise it.

**As to the Drafts Payable Account.**

Even if the practice of the banker in earlier times of setting aside cash of his own to meet drafts drawn upon him were in use today, nevertheless, under the rules above stated, there would be no equitable assignment in favor of the holder of the draft and the instructions to pay could be cancelled at any time. At best he would be holding that cash because of his contractual commitment *to his depositor*, the drawer, and not because of any obligation to the payee.

Despite the wholly clear testimony of Mr. Dawson at folio 368, quoted at length in petitioner's principal brief at page 37 that the foreign bank cancels the advice at the request of the person who has the account in the bank, *whether he is the drawer of the draft or whether he is the person who advised the draft drawn by somebody else*, and despite Mr. Dawson's clear statement that his prior testimony in which he was there speaking of the drawer of the draft where no third party was involved, nevertheless, the claimant now seeks to urge that the foreign bank would only cancel advices where the drawer "wished to have that result accomplished," and that the drawer was not "the person" who had the account in the bank, but the person whose draft was being protected. From this premise, claimant seeks to build up the argument that B. C. I. would cancel an advice only at Trinidad's request and that, therefore, the power to cancel did not rest in the Receiver, or more accurately, did not exist at the time of the filing of the petition. It is needless to review Mr. Dawson's testimony again. This was done at pages 35, *et seq.* of the principal brief. Attention should, however, be called to the stipulation at folio 378:

> "Whenever, prior to the payment of a draft which has been advised abroad in the form of Ex-

hibits 6 to 6E, the *bankrupts* notified the Banca Commerciale Italiana to cancel any specific advice or advices, or to stop payment on any draft or drafts covered therein, Banca Commerciale Italiana forthwith re-credited the *bankrupt's* account with the amount of said draft or drafts, and at the same time debited the account termed 'drafts payable' for the same amount. This was done without knowledge on the part of Banca Commerciale Italiana as to whether such draft or drafts were in the position of the bankrupts, the drawer banks or third parties."

In the light of Mr. Dawson's testimony and the foregoing stipulation, it is again urged there is no justification for the limitations which the respondent seeks to impose on the bankrupt's power or right to cancel advices.

**Absence of Advice to K. N. & K. of Payment of Drafts Immaterial.**

Respondent seeks to make much of the fact that in the drawing service it is stated that the payment of drafts abroad was not usually reported to K. N. & K. and that they could only ascertain whether or not drafts had been presented for payment by making special inquiry to the drawee bank. They also refer to the fact that the statements rendered by the B. C. I. to K. N. & K. show only K. N. & K.'s balance in their general account and not the balance credited to the Drafts Payable Account. Respondent suggests the implication that that was the practice because of the fact that the amounts credited to the Drafts Payable Account were irrevocably appropriated for the payment of drafts. The fact is that the bankrupts having been paid in American dollars, considered that portion of their balance abroad which was credited to the Drafts Payable Account in

the same category as that portion of a bank balance against which a check has been drawn Whether or not the check has been presented, a careful banker considers as the balance available for his business only his "check book balance"—that amount not yet drawn against. This is so, despite the fact that he at any time may stop a check, or even without stopping a check, draw against the balance represented by it, and in the event of his bankruptcy, the balance is not deemed appropriated to outstanding checks.

In the case of drafts advised abroad, either the banker's own drafts or those drawn under "his protection," the banker assumes that both will be presented in due course for payment, and therefore, having advised the foreign bank of the drawing of both kinds of drafts, he is no longer interested in being advised of what his balance is, beyond the balance in excess of the drafts advised. For this reason, there is no need of the foreign bank to render a statement showing anything but the balance over and above the aggregate of advised drafts. But from this fact, it does not follow that the right to cancel advices does not exist. As already shown, that power, in fact, does exist until the foreign bank or the banker here notifies the holder of the supposed equitable assignment by the appropriation of a fund.

Again, reference is made to the fact that certain drafts were not debited to K. N. & K.'s general account and credited to the Drafts Payable Account "through lack of funds" in the general account, and from this fact the inference is sought to be drawn that an actual transfer of funds was intended from one account to the other. But this situation is no different than it would be in the coupon cases or in any case where two accounts are maintained. If, in fact, the funds in the general account were insufficient, then, of course, as a matter of bookkeeping, the other account could not be credited with the amount

of the draft any more than a coupon account could be credited with moneys from the general account, if the latter account, in fact, contained no credit balance.

## The Risk of Loss at All Times Remained With K. N. & K.

At pages 46 and 47 of its brief, respondent asserts that it is interesting to observe that the Trustee has omitted from its brief in this court the question which it asked in the court below, namely, whether the respondent seriously argued that the intention under the drawing service was that the large and small banks throughout the country which had no knowledge of foreign banks, paid over their money relying upon the credit and responsibility of the foreign correspondent unknown to them and chosen by K. N. & K. From this supposed omission, respondent seeks to draw the conclusion that this most potent argument has been abandoned. Had respondent read petitioner's brief with ordinary care, it would have found the question repeated verbatim at the bottom of page 40 of that brief. The answer which the respondent makes to the question is, in fact, no answer at all.

It is stipulated (fol. 70) that the rate fixed by K. N. & K. included a sum estimated as sufficient to compensate K. N. & K. for the service, and of course, in fixing that profit, the danger of the failure of the foreign bank must have been taken into account. It is well known that even where bankers draw their own drafts and where they remain liable as drawers, their profit is exceedingly small in each individual case and is made up by the volume of the business.

Respondent admits at page 63 of its brief, that under the provisions of the drawing service at folio 434, the rate upon which a draft would be *sold* was fixed by K. N. & K. "*upon the same basis*" as the rate upon

which it would agree to *provide for the payment* of drafts drawn under the drawing service, to wit, the market price of the foreign currency involved. This being so, there is, of course, no reason why the obligation assumed under the drawing service should not be as great as in the case where K. N. & K. were liable as the drawers of the draft.

Certainly there is no evidence that the profit which the *Trinidad Bank* made upon the transaction was so large that they, rather than K. N. &. K., could take the risk of the failure of banks upon which they drew drafts. As between the Trinidad or other inland banks and K. N. & K., the latter could certainly afford to take the risk, inasmuch as they had chosen the correspondents and had contacts abroad through which they constantly could be advised as to the necessity of changing their list of correspondents.

**As to Respondents' Authorities.**

In all of the cases relied on by respondent the assignee had knowledge of the appropriation of a *res* to the satisfaction of the obligation due him. In fact he himself had contracted for the appropriation of that *res*. In the present case as has been pointed out the draft-holder —the alleged assignee never had any knowledge of the service contract, the existence of K. N. & K. or of the alleged *res*—the Drafts Payable account. This is a distinction which exists in addition to those already pointed out in petitioner's main brief, at p. 54.

In the *Yardley* case, 165 U. S., 634, it appeared that the equitable assignee itself was informed by the Philadelphia Bank that the New York bank account was in fact the security for the check which had been drawn. Accordingly, the situation was the same as if the legal assignment had, in fact, been made, which of course would

be effective without any consent of the New York bank.

In *Coates* vs. *First National Bank*, 91 N. Y., 20, it appeared that the Masten Bank, being requested to establish the credit in New York for the Salina Bank, advised the Salina Bank that the remittance had been made (91 N. Y., at 22).

In *Muller* vs. *Kling*, 149 App. Div., 176, affirmed 209 N. Y., 239, the transaction was between the assignor and the assignee, and as pointed out by Judge Miller in the Appellate Division, the assignee parted with his money upon the faith and security of an existing debt. So too, in *Hackett* vs. *Campbell*, 10 App. Div., 523, an assignment was delivered to the assignee.

## II.

### As to the Alleged Initial Trust Relationship.

The provisions of the drawing service, which bear on the respondent's contention that the American dollars paid K. N. & K. were initially received in trust, have already been analyzed *in extenso*. The cases relied upon by the respondent are not, generally speaking, cases dealing with foreign exchange transactions and are not even remotely analogous in their facts to the present situation. In addition, they are cases which contain an earlier and different approach to the problem of a banker's obligation, than such recent cases, discussed in the principal brief, as the *Leguia* and *Gravenhorst* cases in New York, the *Beecher* case in Massachusetts, and *Katcher* vs. *American Express Company*, 94 N. J. L. 165 in New Jersey. This fact was recognized by *Mr. Justice Stone* in his article in the *Columbia Law Review* to which reference has already been made, for he says at page 520:

> *"The recent decision of the courts of New York and New Jersey in the case of foreign exchange*

*holding that the obligation of the banker is contractual only, evidence a more just appreciation and exact appraisal of the importance of the method of conducting the banking business in determining what the undertaking of the banker is. The principle of decision in those cases ought to be extended and applied generally to those cases where bankers undertake to effect payments of money for account of their customers in the ordinary course of the banking business whether the exchange element is present or not.*

"The extension of the rule in the *Legniti* case generally to all cases of deposits of funds with a banker for transmission where there is no stipulation that the banker shall keep the deposit segregated as a trust fund, would not in any way limit the application of the rule that, when property other than current funds is received by the banker for account of his customer, it is to be treated legally as a quasi-trust fund. We have already seen that paper entrusted to a banker for collection is so held by him, although he is treated as only a debtor for the proceeds when collected. Bankers do not customarily use such property in their general business as bankers hence there is no custom or practice to rebut the common law presumption that such property is received in a fiduciary capacity."

Even within the scope of their facts, the soundness of the conclusions reached in most of the cases relied upon by the respondent has been questioned by Mr. Justice Stone, for at page 516 of the aforesaid article, he says:

"In many of the United States, on the other hand, the courts, disregarding the customary method of transmitting funds by bankers have applied the usual presumption, when moneys are deposited with a private individual for payment over to a third person and held the depositary liable as a fiduciary. From the application of this rule it follows that the person entitled to the credit is a preferred creditor who may claim

priority of payment over general creditors. And in a number of instances a banker, where an individual, on failing to effect the payment to the payee has been held guilty of embezzlement or of larceny under those modern statutes which are broad enough to embrace embezzlement. He is also subject to civil arrest where that process, as in New York, is applicable in the case of a breach of the fiduciary obligation. There can, of course, be no question but that a fiduciary of moneys who appropriates those moneys to his own use is guilty of embezzlement. *But to hold that a banker receiving money before his known insolvency, for transmission in the ordinary course of the banking business is guilty of larceny merely because of his failure to perform his undertaking or because he has placed the moneys thus received with his general funds and used them as such, would seem to be tantamount to holding that a banker who fails to pay his general depositors or who uses general deposits in his banking business is guilty of larceny.* Criminal liability necessarily follows if the deposit is received in a fiduciary capacity. *But there is no basis for the inference that it is so received if there is no stipulation that the moneys are to be held any differently than other funds deposited with the banker and upon his credit.*"

In the footnote to the comment just quoted there are cited, among others, as a subject of the discussion, the following cases relied upon by the respondent:

*People* vs. *The City Bank of Rochester*, 96 N. Y., 32;

*Cutler* vs. *American Exchange Bank*, 113 N. Y., 593;

*Massey* vs. *Fisher*, 62 Fed., 958.

The foregoing New York cases were pressed upon the New York Court of Appeals in the *Legnitz* case (see

synopsis of argument in that case) and were apparently deemed so inapplicable to the problems arising from the recently developed foreign exchange transactions as not even to require consideration by the Court.

**Rationale of Legniti Case.**

It has already been pointed out in the footnote at page 81 of petitioner's main brief and in the quotation from Mr. Justice Stone's article made in this reply brief, that the imposition of a trust obligation on a banker under any circumstances is questionable. It is clear, however, that the authorities have already restricted the application of such an obligation to those cases which are strictly so-called "transmission" cases, i. e., in which the customer gives to his banker a sum in American dollars, which very sum he desires to have transmitted abroad. Of course he realizes that the payment, when made abroad, will be made in the currency of the country where the payment is made. However, what he desires and contracts for primarily is the transmission of the given amount of American dollars, or *its* foreign equivalent. On the other hand, where the customer contracts with his banker for the payment abroad of a definite amount in foreign currency—where the parties are thinking in terms of a foreign credit in the foreign currency—the sum paid by the customer to the banker is simply the consideration for the payment of the desired and specified foreign amount or for the creation of the desired and specified foreign credit; a sum calculated by the dollar equivalent of the foreign currency amount desired. In the first case the customer in effect says: "Here is $100. Pay it (by means of its lire equivalent) to my mother in Milan." In the second case the customer in effect says: "I want 2,000 lire available to my mother in Milan; here is $100, the dollar equivalent at

existing rates." This is the very distinction at the basis of the *Legniti* case for the Court there said:

> "This was not the case of a specific sum of American money being sent to Naples after being exchanged for lire. It was a case of 18,000 lire being needed in Naples and the purchase of A. Bolognesi's credit with the Banca Commerciale Italiana for this amount * * *"

The Court then held that the situation referred to in the first sentence involving "a specific sum of American money" presented a trust relationship whereas the second situation did not.

Applying the foregoing principles to the present case, it requires no argument to show that Trinidad Bank in effect said to K. N. & K., "We want 24,360 lire available at the Sassari Branch of the B. C. I."—for it had drawn its draft for a definite amount of lire. It therefore could not have been thinking in terms of a specific sum of American dollars but rather in terms of a specific sum of Italian lire.

In the light of this analysis it is urged that there exists no basis for the contention that the American dollars were paid to K. N. & K. for "transmission" to Italy.

The respondent has agreed at page 67 of its brief that the use of the words "principal" and "agent" is not controlling. The sole question, therefore, is what was the relationship resulting from the circumstances. Were the American dollars received in trust for transmission. That they were not, within the test laid down by the *Legniti* case and followed in Massachusetts, has just been shown.

It appears that all the cases relied upon by the respondent were cases where the bank's customer directed the bank to remit or forward a particular sum in American dollars usually for a particular purpose.

In *In re Bolognesi* (C. C. A. 2nd 1918) 254 Fed., 770, upon the bankruptcy of A. Bolognesi & Co., there were presented to the Court the reclamation claims of two distinct classes of creditors—(a) those who had given moneys to the bankrupts for a specific purpose, to wit, either "investment" or transmission abroad, and (b) those who had purchased and received from the bankrupts foreign drafts. In the first class of cases the Court held that the relationship between the customer and Bolognesi was one of trust; that the money was given for investment purposes and that the relationship was no different than that in *Johnson* vs. *Brooks*, 93 N. Y., 337, where the plaintiff gave money to his broker for the purchase of certain named stocks, and the stocks came into the possession of the broker. In the second class of cases, however, where the draft had been purchased and issued, this Court held that the transaction was executed, that the customer procured exactly what he had bargained for, namely, the general obligation evidenced by the draft. That case, therefore, dealt only with situations within classes 1 and 3 analyzed at p. 80 of petitioner's principal brief and in no wise involved a contract for the establishment of a credit abroad.

Similarly, in *In re Jarmulowsky* (C. C. A. 2nd 1919) 258 Fed. 231 the customer gave to the banker $288.00 "to be forwarded" to the customer's designee. This comes clearly within Class 3, for, to use the language of Judge CRANE in the *Legniti* case,

> "it is the amount which he gives that is to be transmitted."

*Farley* vs. *Turner* (1857), 26 L. J. Ch. 710, is fully discussed in petitioner's brief filed in reply to the brief submitted by the Fidelity Trust Company as *amicus curiae*.

In *City of St. Louis* vs. *Johnson* (1879) 5 Dillon 241,

the City of St. Louis handed a check for $173,000.00 to a Missouri bank with a letter which stated

> "which you will please have *remitted to New York* to pay bonds and coupons of the City and County of St. Louis falling due in May proximo."

Here again was a case which in its essence was a transmission case with no obligation to establish a credit but with definite instructions to apply the money to take up the coupons.

That *People* vs. *The City Bank of Rochester* (1884), 96 N. Y., 32, is a remission case and that there money was given for a specific purpose is made clear by the following statement in the Court's opinion at p. 36:

> "The object of the latter was to provide a fund for the payment of specific notes, and the engagement of the former was to apply *that fund* to such payment."

In the case at bar Claimant's Exhibit 4, which contains respondent's instructions to K. N. & K., was a direction merely to "protect" the draft upon presentation and enclosed a check in dollars to pay for that protection "upon presentation." In strict accordance with these instructions Claimant's Exhibit 6 shows that the main office of the foreign bank was merely directed to "protect" the draft and to charge to the account of *K. N. & K.* and the branch was instructed to "honor" the draft and charge the draft to the account of Knauth, Nachod & Kuhne with the main office (Exhibit 6B, fol. 493). Certainly from these documents it is impossible to spell out an engagement or an intention to hold a fund in trust for the payment of the draft. If that had been the intention it would have been very easy for the Trinidad to have said in its advice,

> "We enclose our check for $1,191.20, which please remit to our credit in the B. C. I."

and for K. N. & K. to have directed the establishment of a credit in the name of Trinidad.

In *Cutler* vs. *American Exchange National Bank* (1889), 113 N. Y., 593, the plaintiff, wishing to "remit a sum of money to one Hall in Leadville" paid to the defendant the sum of $500.00 and received in writing a statement addressed to the Bank of Leadville to the effect that the bank's account with the defendant bank had been credited with $500.00 "for the use of J. Seymour Hall." The plaintiff forwarded this letter to Hall and before its receipt the Leadville bank failed. Plaintiff demanded the return of his $500.00 from the defendant which the defendant refused to pay. This case does not differ from the others which the respondent has relied upon. Clearly the money was paid to the defendant bank for the purpose of remission to the Leadville bank for a specific purpose. As above indicated this case was ignored by the Court of Appeals though pressed upon it in the *Legniti* case.

In the last case relied upon by the respondent, *Massey* vs. *Fisher* (C. C. Pa., 1894), 62 Fed., 958, the Court expressly followed the *Bank of Rochester* case and held that where money was deposited with a bank for the specific purpose of using that money to take up the note of a depositor the money was received in trust for that purpose.

## The Foreign Balance Was Not a "Transmuted State of the Money Remitted."

Respondent concedes in its Point III, p. 111, that irrespective of the theory upon which it proceeds, it must trace a specific *res* into the Trustee's possession. In order to accomplish this with respect to the American dollars which respondent claims were paid to K. N. & K. in trust, it is forced to assert in its Point IV, p. 112 that

"the fund abroad was but a transmuted state of the money remitted by claimant to K. N. & K."

Just what this means petitioner is unable to determine. Even if respondent has established the existence of an initial trust, it must then show that the original *res* (the American dollars) or their proceeds (property acquired therewith) is now in the Trustee's possession.

> *Cunningham* vs. *Brown* (1924), 256 U. S., 1, 11;
> *Duel* vs. *Hollins* (1916), 241 U. S., 523;
> *Schuyler* vs. *Littlefield* (1914), 232 U. S., 707.

*For the foreign balance to be the "proceeds" of the American dollars paid, that foreign balance must have been acquired by K. N. & K. by using the very American dollars to purchase the foreign currency credit.* Unless this is shown, there has been no "tracing" within the cases just cited. *There is not a scintilla of evidence in the record to justify this conclusion,* and irrespective of the nature of the relationship, respondent's claim based upon the existence of an initial trust must fail for lack of tracing.

## III.

### The Rights of the Parties were Fixed as of the Filing of the Petition in Bankruptcy.

In petitioner's main brief, Point III, the petitioner argued that under Section 70a (3) and (5) of the Bankruptcy Act, the debt from the B. C. I. to K. N. & K. vested in the Trustee as of the filing of the petition in bankruptcy and that the rights of the parties were fixed as of that date. In its Point V, the respondent "agrees with the petitioner that the rights of the parties became

fixed upon the filing of the petition in bankruptcy and that the subsequent acts of the Receiver cannot change those rights." Despite that "agreement" the respondent at pages 9 to 11 of its brief, attempts to argue that the correspondence between the Receiver and the B. C. I. after the bankruptcy contained admissions against, or in other ways affected, the petitioner's contentions. It is unnecessary here to do anything more than refer to the complete argument made by petitioner in Point III, page 87 of its main brief, and to point out as has been done the inconsistency existing within the Respondent's brief.

The "concession" made by the respondent of the existence of the rule of law that the rights were fixed as of the date of bankruptcy was for the purpose of claiming that the cancellation of the advices by the Receiver after the bankruptcy could not give the estate and the general creditors any rights in addition to those which they had at the time of the filing of the petition in bankruptcy. Petitioner does not claim that the Receiver's acts resulted in any additional rights of the estate. Petitioner's argument set forth at length in the main brief is that since on the date of the filing of the petition in bankruptcy, the bankrupts had the power to cancel the advices and to transfer their balances abroad, those balances were property which passed to the Receiver or Trustee in Bankruptcy and which could be collected by him at his request.

## IV.

### The Correspondence with Thomas B. Paton.

It is hardly conceivable that counsel should have deliberately placed before this Court the correspondence between the Receiver and Thomas B. Paton, Esq., General Counsel of the American Bankers Association, re-

ferred to at pages 90 to 95 of respondent's brief. In the first place that correspondence was never offered in evidence, the Trustee in Bankruptcy was never offered an opportunity to explain or rebut it, and the fact that it was improperly used was pointed out to respondent's counsel when they first presented it in their briefs before the Circuit Court of Appeals. In the second place, when that correspondence was first used before the Circuit Court of Appeals, it became necessary for the Trustee's counsel to print as an appendix to their brief a letter which completed the correspondence between the Receiver and Mr. Paton, which completely disposes of the interpretation placed on the correspondence by the respondent. Despite the fact that this additional letter was made available to the respondent (if it had theretofore been ignorant of it) in petitioner's reply brief before the Circuit Court of Appeals, respondent's counsel now have the temerity again to place before this Court the Paton correspondence, no portion of which is in the record, and again **to leave out any reference to the Receiver's letter** which completely disposes of the alleged admission made by the Receiver, as found in the single letter quoted by respondent.

At page 91 of its brief, respondent quotes from a comment made by Mr. Paton in the August 1923 Journal of the American Bankers Association in reply to an inquiry. At pages 92 *et seq.* respondent quotes from a letter written to Mr. Paton by "the attorneys for the Trustee" (as a matter of fact by the attorneys for the Receiver). In the latter letter it is claimed the Receiver admits that the only question presented by the case now before this Court is whether the admittedly deposited trust funds could be traced into the Receiver's or Trustee's possession.

Reluctantly the petitioner burdens this Court with a quotation from the appendix to the Trustee's brief be-

fore the Circuit Court of Appeals, commenting upon the respondent's use of the Paton material:*

> "In so far as the appellant attempts to rely upon the letter of the receiver and his counsel as an *admission* of the soundness of the position now taken by the appellant, the facts are as follows: After the publication of Mr. Paton's article in the *August* 1923 Journal, counsel for the receiver wrote the letter dated September 20, 1923, from which the appellant has quoted, (although the letter is not in evidence and although of course admissions by the receiver with whom claims are not filed are of not the slightest significance). In reply to that letter and prior to its publication Mr. Paton supplied the receiver and his counsel with proof of his proposed article to appear in the *November* 1923 number of the Journal which article included a quotation in full of the receiver's letter of September 20th. After quoting that letter Mr. Paton, in his consideration of the receiver's position, stated:
>
> > 'The argument of the receiver and his attorney virtually concedes, without prejudice, that where a single remittance is made to a banker for a special purpose and the remittance is mingled with the banker's general fund in his own vaults or in bank which passes to a receiver upon its failure, the purpose not being carried out, the remittance is a trust fund the identity of which is not lost by the mere mingling, but it remains identifiable and recoverable in full if the mingled fund from the time of the receipt of the remittance to the time of the receiver taking possession equals or exceeds the amount of the remittance, or if the fund remaining is less than the remittance, then the trust attaches to what remains.'

*The term "appellant" in the following quotation refers to the respondent in this court.

"In acknowledging the receipt of Mr. Paton's letter with the proof of his proposed article the receiver and his counsel took exception to the assumption made by Mr. Paton, and now again advanced by the appellant, and said in a letter to Mr. Paton, under date of November 5, 1923, *to which the appellant has made no reference*:

> 'In further reply to your interesting letter of November 1st with which you enclose a copy of your opinion in the November number of the Journal of the American Bankers Association, *we wish to take exception* to a statement appearing in the first column of the second page of that opinion, under a heading entitled "Case of Single Remitter."
>
> 'You state that "the argument of the Receiver and his attorney virtually concedes, without prejudice, that where a single remittance is made to a banker for a special purpose, and the remittance is mingled with the banker's general funds in his own vaults or in banks, which pass to the Receiver upon its failure, the purpose not being carried out, the remittance is a trust fund * * *"
>
> 'Without at this time discussing the case involving cable transfers and money orders, and limiting ourselves to the draft situation which was originally involved, **we do not concede the result referred to.** There appears to be little doubt that where as a fact, it is determined that moneys are remitted to the banker for a special purpose, such moneys become trust funds. However, we by no means concede, that a purchaser of a draft in remitting payment therefore is depositing money for a special purpose within that rule of law. In fact, all of the authority which we have been able to find is to the contrary, and we are pleased to refer you to what we consider the leading cases on the subject, to wit:

*In re A. Bolognesi & Co.*, 254 Fed. 770;
*Weideman* vs. *Newton*, 271 Fed. 302;
*Lowell* vs. *Brown*, 284 Fed. 936, 941;
*Legniti* vs. *Mechanics & Metals National Bank*, 230 N. Y., 415.

We thought it best to make this statement to you before your conference with us, so that you might be prepared to discuss this legal question should it arise.'

"Inasmuch as the respondent did not adopt the usual procedure of offering in evidence at the hearing before the Master the letter upon which it now desires to rely and in which it claims is an admission against the estate, the Trustee of course has had no oportunity to place before any Court the letter of November 5th just quoted which clearly shows that even as a matter of pure fact no admission was made by the receiver, 'virtually' or otherwise, immaterial as it might be."

Respectfully submitted,

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Office Supreme Court, U. S.
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# Supreme Court of the United States

OCTOBER TERM, 1927.
No. 130

THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy of KNAUTH, NACHOD & KUHNE,

*Petitioner,*

*against*

THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO,

*Respondent.*

## BRIEF FOR PETITIONER

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# SUBJECT INDEX.


PAGE

The Opinions Below ..... 1
The Grounds of this Court's Jurisdiction ..... 2
The Present Case Important as a Test Case ..... 2
Statement of the Salient Facts, Showing the Successive Steps in the Transactions Between the Trinidad Bank and the Bankrupts, K. N. & K. ..... 3
The Theory of the Claim of the Trinidad Bank ..... 8
The Contentions of the Trustee in Bankruptcy ..... 9
The Holdings Below in the Present Case and in Related Cases ..... 11
Conflicting Theories of the Trinidad Bank and of the amicus curiae, Fidelity Trust Company of New York ..... 13
Desirability of an Opinion on All Points Presented ..... 14


## Brief of Argument.


POINT I. Neither the contract of the parties nor any of the acts done by K. N. & K. or the B. C. I. after the receipt of the American Dollars by K. N. & K. were intended to constitute or did constitute an equitable assignment of K. N. & K.'s balance in the B. C. I. as alleged in the respondent's second cause of action ..... 15
A. Tests of Equitable Assignments ..... 16
B. The Necessary Results of Respondent's Contentions ..... 20
C. Neither the Provisions of the Drawing Service Nor the Acts Done in the Performance of K. N. & K.'s Obligations Were Intended to or Did Constitute an Equitable Assignment 22
1. The Provisions of the Drawing Service, and the Forms Provided for Use therewith, do not Disclose any Intention that any "Fund" Should Be Created in Advance or Assigned for the Payment of the Draft Drawn by Trinidad on the B. C. I. ..... 22
Effect of Direction of Trinidad to K. N. & K. to Protect Draft on Presentation ..... 23
Wabash St. Louis & Pacific Railroad Co. vs. Ham, 114 U. S. 587 ..... 24
The Instructions of K. N. & K. to its Correspondent—B. C. I. ..... 25
Nature of Obligation to Provide Drawee with "Funds Sufficient for the Payment of the Draft" 27

PAGE

2. The Acts Done by K. N. & K. and by the B. C. I. in the Performance of K. N. & K.'s Obligation under the Drawing Service, Including the Bookkeeping Entries Made by the B. C. I. Pursuant to a Well Established International Banking Custom, Are no Evidence of an Intention to Assign or Appropriate a Fund. This is particularly so, inasmuch as K. N. & K. at all Times Retained Control of their Balance and Had the Right to Cancel Advices, and thus Remained the Creditor of B. C. I. ... 29

The Debiting by B. C. I ... 30

Testimony of Dawson as to Reasons for Existence of "Drafts Payable Account." Its Creation Independent of Drawing Service Contract ... 32

K. N. & K. at all Times Remained the Owner of and in Control of the Balance in the Drafts Payable Account for They Could Always Have Cancelled the Draft ... 35

The Forms Used for Cancellation ... 37

Other Evidence Confirming Dawson's Testimony as to Custom ... 38

D. The Conclusions from the Foregoing Facts Show that the Tests of the Existence of Equitable Assignments Have Not Been Met ... 39

E. The Errors of the Court Below ... 42

Summary ... 47

F. Leading Cases on Equitable Assignments and the Tests as to Their Creation ... 48

The Noyes Case, 140 App. Div., 162; 224 N. Y. 542 ... 48

The Erb Case, 243 N. Y., 45 ... 50

The Interborough Consolidated Case, 288 Fed., 334 ... 51

Summary of Noyes and Interborough Cases ... 53

G. Authorities Relied on by Respondent and Court Below Distinguished ... 54

Fourth National Bank vs. Yardley, 165 U. S., 634 ... 54

Coates vs. First National Bank of Emporia, 91 N. Y., 29 ... 55

Muller vs. Kling, 149 App. Div., 176 ... 55

Hackett vs. Campbell, 10 App., 523 ... 56

Dean (now Mr. Justice) Stone's Discussion ... 56

Conclusion to Point I ... 57

Point II. The contract of the parties and the method of its execution did not establish ab initio a fiduciary or agency relationship between the Trinidad Bank and K. N. & K. ... 58

Preliminary Statement ... 58

A. Fundamental Legal Principles Underlying the Agency Relationship ... 59

PAGE

B. The Evidence of an Independent Contractor Rather Than an Agency Relationship ..... 59

C. The Use of the Words "Principal" and "Agent" Are Not Controlling and Do Not Negative the Conclusion that the Parties Dealt as Independent Contractors ..... 64

Reasons for the Use of the Terms "Principal" and "Agent" in the Present Contract ..... 67

No Technical Agency ..... 68

D. Leading Recent Cases Holding that the Relationship Established Was Not a Fiduciary One ..... 71

Beecher vs. Cosmopolitan Trust Co., 239 Mass., 48 ..... 71

Equitable Trust Co. vs. Keene, 232 N. Y., 290 ..... 74

Legniti vs. Mechanics & Metals National Bank, 230 N. Y., 415 ..... 74

Taussig vs. Carnegie Trust Company, 156 App. Div., 519 78

Kuehne vs. Union Trust Company, 133 Mich., 602 ..... 79

E. Principles Deducible from the Foregoing Authorities as to Existence of Fiduciary Relationship ..... 80

F. Obligation of K. N. & K. Even Less Susceptible of Interpretation as a Fiduciary Obligation than Bankrupt's Obligation in Legniti and Beecher cases ..... 85

G. The Hutchins Case in this Court (231 U. S., 50) Has Clearly Recognized the Principles Underlying the Trustee's Contentions ..... 85

Conclusion to Point II ..... 86

POINT III. Under Section 70a (3) and (5) of the Bankruptcy Act, the debt from B. C. I. to K. N. & K. vested in the Trustee as of the date of the filing of the petition in bankruptcy. The rights of the parties became fixed upon that date and the subsequent acts of the Receiver cannot change those rights. But the subsequent acts of B. C. I. are most persuasive evidence of the soundness of the Trustee's contentions ..... 87

Everett vs. Judson, 228 U. S., 474;

Fairbanks Shovel Co. vs. Wills, 240 U. S., 642;

Cohen vs. Samuel, 245 U. S., 50.

POINT IV. The general object of the Bankruptcy Laws is to afford equality among all creditors remaining unpaid at the date of the bankruptcy and in order to obtain equitable relief or to establish a right to specific funds, the Courts have been strict in demanding that the claimant's right be founded upon the clear intention of the parties without vagueness or uncertainty. The respondent here has failed to sustain that burden ..... 89

Westinghouse El. & Mfg. Co. vs. Brooklyn R. T. Co., 263 Fed., 532

In re Stiger, 209 Fed., 148.

The Vagueness of Respondent's Case ..... 90

POINT V. In Conclusion ..... 91

# TABLE OF CASES.


PAGE

Aetna National Bank vs. Fourth National Bank, 46 N. Y., 82 ..... 19
American Express Co. vs. Cosmopolitan Trust Co., 239 Mass., 249 81
Barnes vs. Alexander, 232 U. S., 117 ..... 17
Beecher vs. Cosmopolitan Trust Co., 239 Mass., 48 ... 27, 62, 65, 71, 81, 85
Bendix vs. Staver Carriage Co., 174 Ill. App., 589 ..... 65
Bolognesi, In re, 254 Fed., 770 ..... 65, 80
Casement vs. Brown, 148 U. S., 615 ..... 65
Cheney vs. Libbey, 134 U. S., 68 ..... 19
Christmas vs. Russell, 14 Wall., 69 ..... 18, 19
Coates vs. First National Bank, 91 N. Y., 20 ..... 55
Cohen vs. Samuel, 245 U. S., 50 ..... 89
Cushings vs. Chapman, 115 Fed., 237 ..... 18
Eastman Kodak Co. vs. Park National Bank, 231 Fed., 329 ..... 19, 25
Empire Trust Co. vs. Cahan, 71 L. Ed., 820 ..... 51, 74
Employers' L. A. Corp. vs. U. S. S. B. E. Fleet Corp., 290 Fed., 182 65
Erb vs. Banco di Napoli, 244 N. Y., 45 ..... 27, 50
Equitable Trust Co. vs. Keene, 232 N. Y., 290 ..... 74
Everett vs. Judson, 228 U. S., 474 ..... 88
Fairbanks Shovel Co. vs. Wills, 240 U. S., 642 ..... 88
Foreign Trade Banking Corp. vs. Cosmopolitan Trust Co., 240 Mass., 413 ..... 81
Fourth National Bank vs. Yardley, 165 U. S., 634 ..... 54
Fowble, In re, 213 Fed., 676 ..... 91
Gravenhorst vs. Zimmerman, 216 N. Y., 22 ..... 77, 81
Gubelman, In re, Ex parte Muntean, 13 Fed. (2d) 730 ..... 12, 47
Hackett vs. Campbell, 10 App. Div., 523 ..... 50
Hamer vs. Sidway, 124 N. Y., 538 ..... 16
Hopkinson vs. Forster, L. R. 19, Eq. 74 ..... 16, 20
Interboro Consolidated Corp., In re, 288 Fed., 354 ..... 16, 17, 20, 51, 53
Kuehne vs. Union Trust Co., 133 Mich., 602 ..... 20, 79
Legnitti vs. Mechanics & Metals Nat'l Bank, 230 N. Y., 415 ..... 56, 74, 80, 81, 82, 85, 91
Moore vs. Potter, 155 N. Y., 481 ..... 66
Muller vs. Kling, 149 App. Div., 176 ..... 55
Musco vs. United Surety Company, 132 App. Div., 200 ..... 82
National City Bank vs. Hotchkiss, 231 U. S., 50 ..... 19, 31, 85, 86
Noyes vs. First Nat'l Bank, 180 App. Div., 162 ..... 20, 48, 53
Robbins vs. Robinson, 176 Pa., 341 ..... 25
Safian vs. Irving Nat'l Bank, 202 App. Div., 459 ..... 78
St. Regis Paper Co. vs. Hubbs &c. Paper Co., 225 N. Y., 50 ..... 65
Samuels vs. E. F. Drew & Co., 206 Fed., 882 ..... 78
Sloan Shipyards Corp. vs. U. S. S. B. E. Fleet Corp., 258 U. S., 549 ..... 65, 66
Spellman vs. Bankers' Trust Co., 6 Fed. (2d) 799 ..... 17, 18
Stiger, In re, 202 Fed., 791 ..... 18, 90
Strohmeyer & Arpe Co. vs. Guaranty Trust Co., 172 App. Div., 16 ..... 77

PAGE
Taussig vs. Carnegie Trust Co., 156 App. Div., 519 ..... 20, 50, 78
Tiernan vs. Jackson, 5 Peters, 579 ..... 17
Tindal, In re, 155 Fed., 456 ..... 91
Wabash St. L. & Pac. Ry. Co. vs. Ham, 114 U. S., 587 ..... 24, 61
Westinghouse El. & Mfg. Co. vs. Brooklyn R. T. Co., 263 Fed., 532 ... 89
Williams vs. Everett, 14 East, 581 ..... 17
Williams vs. Ingersoll, 89 N. Y., 508 ..... 19
Williams, Petition of, 297 Fed., 696 ..... 65
Zimmerman & Forshay, Matter of, 14 Fed. (2d), 527 ..... 12, 44, 45, 88
Zotti, People ex rel vs. Flynn, 135 App. Div., 276 ..... 82

## Other Authorities Cited.

Bankruptcy Act, Section 70a (4) and (5) ..... 87, 88
Section 47a (2) ..... 89
Columbia Law Review, vol. 20, p. 333 ..... 70
vol. 22, p. 576 ..... 70
Corpus Juris, vol. 2, p. 423 ..... 65
vol. 5, p. 913 ..... 18
vol. 30, p. 457 ..... 26
Funk & Wagnall's New Standard Dictionary—"Protect" ..... 25
Huffcut—Agency, 12 ..... 70
Mechem, Agency, Secs. 25 and 40 ..... 69
Pomeroy Eq. Jurisprudence (4th Ed., 1918), Vol. 3,
Sec. 1281 ..... 16, 47
Sec. 1282 ..... 19
Stone's Discussion, Dean (now Mr. Justice) in 21 Columbia Law Review, 507 ..... 56, 65, 81, 82, 83
Story's Commentaries on Equity, Section 1045 ..... 17
Webster's New International Dictionary, 1924—"Protect" ..... 24

# Supreme Court of the United States

OCTOBER TERM—1927.

THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy of Knauth, Nachod & Kuhne,
Petitioner,

*against*

THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO,
Respondent.

## BRIEF FOR PETITIONER.*

This case comes to this Court on a writ of *certiorari* to the Circuit Court of Appeals for the Second Circuit whose decree reversed a decree of the United States District Court for the Southern District of New York. The decision of the Circuit Court of Appeals allowed the reclamation claim of the respondent, The First National Bank of Trinidad, Colorado, (hereinafter referred to as the Trinidad Bank) against the estate in bankruptcy of Knauth, Nachod & Kuhne (hereinafter referred to as "K. N. & K.").

### The Opinions Below.

The opinion of the Special Master and of the District Court disallowing the reclamation claim are not officially

*The italics throughout have been inserted by counsel.

reported, but appear at folios 598 and 667 of the Record. The opinion of the Circuit Court of Appeals reversing the decision of the District Court is reported in 13 Fed. (2d) 732.

**The Grounds of this Court's Jurisdiction.**

The jurisdiction of this Court is based upon a writ of *certiorari* which on November 23, 1926, was granted under Judicial Code Section 240 (A) as amended by the act of February 13, 1925, to review a final decree entered on July 13, 1926 (fol. 772) in the bankruptcy proceedings of K. N. & K.

**The Present Case Important as a Test Case.**

This is a test case. There are pending undetermined in the District Court approximately two hundred and twenty reclamation claims similar in varying degrees to the present one, filed on behalf of various inland banks and bankers. Those petitions seek to recover the aggregate sum of approximately $800,000 which it is asserted came into the possession of the trustee in bankruptcy, the petitioner herein. The claimants insist that the sums sought to be recovered are not part of the bankrupts' estate but in equity belong to them. Accordingly the reclaimants seek to have their claims paid in full out of these funds rather than have their claims share *pro rata* with all the general creditors of the bankrupts. Of these claims, approximately two hundred are represented by the attorneys for the present respondent and a list of the various banks and bankers throughout the country represented by them appears in the stipulation annexed to the reclamation petition herein (fol. 25).

The facts with respect to all of such other claims are not, however, identical with those of the case at bar. The facts with respect to the claim of the Fidelity Trust

Company of New York are typical of one of the groups of claims pending undetermined, which differ in one important fact from the present case. Accordingly the Fidelity Trust Company, pursuant to leave obtained, has filed a brief herein as *amicus curiae*. For convenience, the petitioner will reply to the brief *amicus curiae* in a separate brief to be filed herein.

It is hoped that the ultimate determination of the claim of the Trinidad bank will make unnecessary the trial of the other claims. To that end petitioner respectfully urges this Court to include in its opinion a discussion of both causes of action set forth in the Respondent's petition as well as of the theory advanced in the brief of the *amicus curiae*.

## Statement of the Salient Facts, Showing the Successive Steps in the Transactions Between the Trinidad Bank and the Bankrupts, K. N. & K.

The transaction from which the controversy here arose was not a single, particular, exceptional or isolated one. It was one of literally thousands of similar transactions which the bankrupts and innumerable banks and dealers in foreign exchange were parties to daily.

K. N. & K., prior to their failure in June, 1923, were large dealers in foreign exchange. They maintained large foreign balances and in their own name issued large numbers of foreign drafts.

The First National Bank of Trinidad, Colorado (hereinafter referred to as the Trinidad bank) and the numerous other inland banks and bankers maintained no foreign balances, had no foreign correspondents and had no facilities for directly drawing and selling drafts on foreign banks and bankers. In order to enable the inland banks to issue drafts in their own names and, perhaps, to impress their customers with the facilities which the

banks were able to offer, K. N. & K. offered a "Drawing Service," under which the various inland banks could draw *their own drafts* on foreign correspondents listed by K. N. & K. just as if the inland banks did have foreign correspondents; and K. N. & K. undertook to provide sufficient funds for the payment of such drafts abroad (fols. 420, 423, 474).

In summary, the arrangement was as follows:

(1) K. N. & K. sent to their inland bank correspondents, including the Trinidad bank, daily rate cards fixing the rate for the various foreign currencies (Italian lire in this case) under the Drawing Service (fols. 70, 434). The rates quoted were "good" only during the day printed on the cards (fol. 434).

(2) Upon the request of its customer in Colorado, the Trinidad bank would sell *its own draft* on one of the foreign correspondents named in K. N. & K.'s list, for the desired amount of foreign currency, and would receive payment therefor at the rate fixed in the rate card, plus whatever profit the Trinidad bank sought to charge its customer. *The name of K. N. & K. did not appear on the draft. So far as the bank's customer knew*, the Trinidad bank maintained direct relations with the foreign correspondent (fols. 70-72).

(3) Immediately upon the issuance of the draft, the Trinidad bank would send to K. N. & K. an advice (Claimant's Exhibit 4, p. 161), of the drawing of the draft, requesting K. N. & K. "to *protect* same *upon presentation*." With the advice was sent a sum in American dollars at the rate fixed in the rate card.

(4) Upon receipt of the advice and check, the check was deposited in one of the general checking accounts of

K. N. & K., in the Guaranty Trust Company in this case (fol. 74).

(5) On the day that the advice was received from the Trinidad bank, K. N. & K. also sent its advice to the foreign bank upon which the draft had been drawn by the Trinidad bank, including in such advice not only all drafts which had been drawn that day on that foreign correspondent of K. N. & K. by all *other* inland banks availing themselves of the Drawing Service, but also drafts drawn *by K. N. & K. themselves*. All the advices to one foreign correspondent which went forward by one steamer were known as a "Steamer Block" (fol. 75).

(6) The "Steamer Block" was in two parts—(a) one advice to the main office of the foreign drawee, and (b) an individual advice to each branch of the foreign drawee upon which drafts had been drawn that day (fol. 76). The advice to the *main office* of the foreign bank upon which the draft was drawn (the Banca Commerciale Italiana in this case, hereinafter for convenience referred to as B. C. I.) requested the B. C. I. "to *protect* to the debit of *our* account the drafts as per particulars on the attached copies" (Claimant's Exhibit 6, p. 163). Attached to the foregoing, were copies of the advices which had been sent to the *branches* of the B. C. I. (Claimant's Exhibits 6A, 6B, 6C, 6D, 6E). The particular draft here involved is found in the advice sent to the Sassari Branch of the B. C. I. (Exhibit 6D). This advice to the branch banks contains the following direction:

> "Please *honor* the above listed drafts charging same to *our* account with Banca Comm. Italiana Genoa."

(7) When the B. C. I. received the above mentioned advices, it thereupon debited the account which K. N. & K.

maintained with the bank at its Genoa office to the extent of the aggregate of the drafts, and simultaneously credited on its books an account termed "Drafts Payable," in which account were also credited amounts of drafts which were advised to the B. C. I. for payment by other depositors or clients of the B. C. I. (fol. 92). Thereafter, no interest was allowed to K. N. & K. or to anyone else upon the amount credited to the Drafts Payable Account, but on the other hand, the B. C. I. received no compensation for its services in honoring drafts except the compensation measured by its use, without the payment of interest, of the money in the Drafts Payable Account (fol. 93).

(8) *All drafts were thus dealt with* whether drawn by K. N. & K. themselves or drawn by their inland correspondents (See Claimant's Exhibit 6A, fol. 490, which includes advice of drafts issued by "Ourselves").

(9) It appears in evidence *without contradiction* that there is a well recognized banking custom of long standing, under which the foregoing practice is pursued, and that the reasons for the practice are that by making such bookkeeping entries (a) the drawee bank at all times knows of its possible demand obligations and can keep itself in a position to meet the drafts which have been advised, and (b) as sole compensation for its services in the transaction, it is enabled to use the funds during the interval before the presentation of the drafts without paying interest thereon (fols. 93, 359).

(10) It also appears without contradiction from the testimony of the expert Dawson, Vice-President of the Guaranty Trust Company of New York, that under the foregoing well established banking custom and practice, the American depositor who has an account in the for-

eign bank *may cancel the advice* of a draft *drawn either by himself or by his inland correspondent*, without obtaining the consent of the payee of the draft or the inland correspondent, and that the foreign bank recognizes and obeys only the orders of its own client without inquiring as to any one's else instructions (fol. 368).

On this point it was stipulated (fol. 378):

> "Whenever, prior to the payment of a draft which has been advised abroad in the form of Exhibits 6 to 6-E, the bankrupts notified the Banca Commerciale Italiana to cancel any specific advice or advices, or to stop payment on any draft or drafts covered therein, Banca Commerciale Italiana forthwith recredited the bankrupts' account with the amount of said draft or drafts and at the same time debited the account termed 'Drafts Payable' for the same amount. This was done without knowledge on the part of Banca Commerciale Italiana as to whether such draft or drafts were in the possession of the bankrupts, the drawer banks or third persons."

It also appears that B. C. I. cancelled drafts at the request of K. N. & K. without being informed that the cancellation was made upon the request of the Trinidad Bank (fol. 222). While it was also stipulated (fol. 379) that in the case of the present respondent, K. N. & K. had never cancelled an advice without a previous request to do so from respondent, this has no bearing on the question of K. N. & K's. relations with their foreign correspondents and K. N. & K's. control over their foreign balances. It should also be noted that K. N. & K. had regular forms for cancelling advices used for both their own and inland bank drafts (Trustee's Exhibits 3 and 4, p. 192 and fol. 383). *Thus it appears that at all times K. N. & K. kept control over their foreign balances and could cancel the advices as they saw fit.*

(11) There is no evidence that the draft holder had knowledge of the existence of the Drafts Payable Account or of the existence of the Drawing Service.

(12) In the present case, the advice of the Trinidad draft was not cancelled prior to the filing of the petition in bankruptcy, but immediately upon the appointment of the receiver, he cabled to the B. C. I. that he had taken possession of the assets and that all of the bankrupt's credit balances must be held subject to his order (Claimant's Exhibit 10, fol. 520). Thereafter the B. C. I. acquiesced in the Receiver's view that the balances in the Drafts Payable Account belonged to the bankrupts and such balances in the general account of K. N. & K. with the B. C. I. *and the balances in the drafts payable account* were returned to the receiver by the B. C. I.

(13) *After* the bankruptcy, the draft was presented to the drawee and payment refused (fol. 330). Thereupon the draft was returned to the purchaser thereof and the Trinidad bank paid to such purchaser the purchase price thereof and received the draft (fol. 330).

**The Theory of the Claim of the Trinidad Bank.**

The reclamation petition of the Trinidad Bank (fol. 1) asserts a right to recover specific moneys which came into the possession of the trustee in bankruptcy under the following two distinct counts or causes of action:

(A) That by the terms and conditions of the Drawing Service the American dollars which the respondent paid to K. N. & K., as described in paragraph (3) above, were initially received by K. N. & K. in trust and that said funds have in fact come into the possession of the trustee.

(B) That pursuant to the terms of the Drawing Service, K. N. & K. had equitably assigned the portion of its balance in the B. C. I. which had been credited on the latter's books to the Drafts Payable Account (under the circumstances described in paragraph (7) above) and that the amount of that credit has been returned to the trustee in bankruptcy by the B. C. I. as set forth in paragraph (11) above, and is the property of the respondent.

**The Contentions of the Trustee in Bankruptcy.***

The trustee in bankruptcy contends:

(*a*) That K. N. & K. were acting as *entrepreneurs* who, in consideration of American dollars paid in advance, assumed an executory obligation to "protect the draft *on presentation.*" That is K. N. & K. undertook to have a sufficient balance in lire at the Italian bank, the B. C. I., upon the presentation of the draft of the Trinidad bank, so that the draft would be "honored" upon such presentation to the debit of K. N. & K.'s balance in pursuance of ordinary banking practices and in the same manner as the drafts which K. N. & K. themselves drew would be honored.

(*b*) That the arrangement of the parties did not contemplate that a fund should be set up *in advance* which should be the sole source for the payment of the Trinidad bank's drafts. The arrangement contemplated that K. N. & K. would protect the draft on its *presentation*, i. e., would see to it that the draft was *paid*.

(*c*) The *acquiescence* by K. N. & K. in the foreign bank's practice of charging K. N. & K.'s account on the receipt of the advice and crediting the Drafts Payable Account was not intended to constitute performance

*A complete Brief of the Argument is included in the Index.

of K. N. & K.'s obligation or an appropriation in advance of a fund from which the draft was to be paid. For the same practice was pursued with respect to drafts drawn by K. N. & K. themselves where clearly there was no conceivable obligation to provide a fund in advance, inasmuch as they were not drawing pursuant to any special contract like the "Drawing Service." Furthermore, as above pointed out, K. N. & K. at all times remained in complete control of their entire balance including that portion credited in the Drafts Payable Account.

(*d*) The uncontradicted evidence shows that the practice of crediting the Drafts Payable Account existed independent of any "Drawing Service" and for wholly different reasons.

Answering specifically the claims of the Trinidad Bank as set forth in its reclamation petition, the trustee in bankruptcy contends:

(1) That under the terms of the Drawing Service and the forms provided therewith, no trust relationship arose between the Trinidad Bank and K. N. & K.

(2) That the parties dealt as independent contractors and that the moneys paid to K. N. & K. by the Trinidad bank were paid for K. N. & K.'s obligation to produce a certain result, namely, the honoring of the draft by B. C. I. upon its presentation. In short K. N. & K. agreed to protect, in the same manner as drafts drawn by themselves, the drafts drawn by the Trinidad or other inland banks.

(3) That there was no agreement to assign any funds abroad and that the acts of K. N. & K. after the receipt of the American dollars, did not result in an equitable assignment; that these acts were done solely in pursuance of the banking practice already described.

(4) That the balance in the B. C. I. which is sought to be reclaimed remained the property of and was always wholly within the control of K. N. & K. and K. N. & K. alone was the creditor of the B. C. I. Prior to the filing of the petition in bankruptcy the balance in the Drafts Payable Account was property which the bankrupts "could by any means have transferred," by exercising the power of revocation and accordingly was property which vested in the Trustee in Bankruptcy pursuant to Section 70 (a) (3) and (5) of the Bankruptcy Act.

(5) The general object of the Bankruptcy Laws is to afford equality among all creditors remaining unpaid at the date of the bankruptcy and in order to obtain equitable relief or to establish a right to specific funds, the courts have been strict in demanding that the claimant's right be founded upon the clear intention of the parties without vagueness or uncertainty. The respondent here has failed to sustain that burden.

**The Holdings Below in the Present Case and in Related Cases.**

Three cases, involving in some of their aspects the problems here presented, were before the Circuit Court of Appeals for decision at the same time. In the present case that Court held that the credit to the Drafts Payable Account by the foreign bank when it received K. N. & K.'s advice of the drawing of the draft by Trinidad constituted a "performance" by K. N. & K. of its obligation under the Drawing Service; that it was for the benefit of the *holder of the draft* and constituted an equitable assignment to him of the balance so credited and a discharge of K. N. & K. And it held, further, that the Trinidad bank having taken up the draft by paying the

holder acquired the rights of such holder. Having reached this conclusion, the Court found it unnecessary to determine whether or not K. N. & K. had initially received the American dollars from the Trinidad bank in trust. A detailed analysis of the Circuit Court's opinion appears at page 42 *post*.

On the same day that the case at bar was decided in the Court below, that Court decided *Matter of Zimmerman & Forshay, Ex parte Henry G. Gray*, 14 Fed. (2d) 527. In that case the bankrupts, Zimmerman & Forshay, sold to Gray a draft which *they themselves* had drawn on a foreign bank with which they maintained a balance. *There was no special contract similar to the Drawing Service used in the present case.* The draft was advised abroad, charged to the bankrupts' account and credited to a Drafts Payable Account in the same manner as in the case at bar. There, as here, the advice was cancelled after the bankruptcy and before the draft was presented and there, as here, the funds were returned to the receiver in bankruptcy. In that case it was also stipulated that the dealings between the bankrupts, Zimmerman & Forshay, and the foreign bank were such that when the bankrupts drew the draft on the foreign bank "and later for any reason wished to stop payment that a direction to stop payment will be honored by the bank." Despite the absence of even the semblance of a special agreement for the creation in advance of a special fund to meet the check, the Court below nevertheless held that the claimant was entitled to recover the moneys which had been returned to the receiver in bankruptcy. It was forced so to hold to remain consistent with its decision in the present case. (See p. 44 *infra*.)

Also on the same day the Court below handed down its decision in *In re Gubelman, Ex parte Munteau*, 13 Fed (2d) 739. That case arose in this same bankruptcy proceeding of K. N. & K. A general claim had been

filed by Muntean, the holder of a draft issued by an inland bank under the same Drawing Service as that used by the Trinidad bank in the present case. After payment of the draft had been refused abroad, instead of presenting that draft to the inland bank which had issued it, the holder, Muntean, filed a general claim directly with the bankrupt estate. The trustee objected to the claim on the ground that there had been no contractual relationship between K. N. & K. and the holder of the draft and that, therefore, the holder of the draft had no provable claim in bankruptcy. In other words, the trustee asserted that the claim was based on the theory that the contract between the inland bank and K. N. & K. had been made for the benefit of the holder of the draft issued by the inland bank. The Circuit Court of Appeals, however, held that the facts in the *Muntean* case were not within the Federal third party beneficiary doctrine inasmuch as the contract between K. N. & K. and the inland bank had not been made primarily for the benefit of the draft holder but rather for the benefit of the inland bank itself.

As will be shown hereafter, the foregoing decisions handed down on the same day as the one in the case at bar are important because they will make clear the errors which underlie the determination of the Court below in the present case.

**Conflicting Theories of the Trinidad Bank and of the amicus curiae, Fidelity Trust Company of New York.**

As has been shown, the theory advanced by the Trinidad bank and adopted by the Court below was that because of the credit to the Drafts Payable Account abroad, the balance in that account had been equitably assigned

to, or irrevocably appropriated for, the benefit of the holder of the draft, to whose position the Trinidad bank was thereafter subrogated by its taking up the draft. The Fidelity Trust Company on the other hand, in its brief filed herein as *amicus curiae*, not being in a position to show a credit to the Drafts Payable Account abroad, has been forced to contend that the mere advice by K. N. & K. to the foreign bank, when received abroad, worked an equitable assignment of an aliquot part of, K. N. & K.'s foreign balance in favor, *not of the draft holder, but of the drawer bank.*

This conflict evidences the attempt of the banks contracting with K. N. & K., after the latter's bankruptcy, to secure for themselves on one theory or another a position entitling them to priority in payment, to the detriment of the general creditors of the bankrupt estate.

**Desirability of an Opinion on All Points Presented.**

In view of the fact that this is a test case, decision in which it is hoped will dispose of many reclamation claims and lead to a prompt termination of litigation, petitioner respectfully requests that this Court express its views not only upon both causes of action set forth in the Trinidad bank's petition but also on the theory advanced in the brief of the Fidelity Trust Company as *amicus curiae*.

Since, however, the decision below is based entirely on the Trinidad bank's second cause of action, i. e., that there had been an equitable assignment—the petitioner-trustee will first discuss that conclusion.

## POINT I.

**Neither the contract of the parties nor any of the acts done by K. N. & K. or the B. C. I. after the receipt of the American dollars by K. N. & K. were intended to constitute or did constitute an equitable assignment of K. N. & K.'s balance in the B. C. I. as alleged in the respondent's second cause of action.**

In considering the respondent's second cause of action in which an equitable assignment is alleged, the Trustee will

A. State the legal principles applicable to equitable assignments.

B. Indicate what the respondent's contentions are and what their necessary results must be.

C. Show that there was initially no intention or obligation to make an assignment of any fund in advance of the presentation of the draft—which will involve an analysis of the contract of the parties.

D. Analyze the acts of K. N. & K. and the B. C. I. after the receipt of the American Dollars by K. N. & K. and show that the acts of both of these parties were not intended to constitute an equitable assignment of any fund in pursuance of any contract, but were done merely in pursuance of well established banking practices under which the credit always remained the property of and under the control and subject to the disposition of K. N. & K. until the presentation and payment of the drafts.

E. Analyze the opinion in the Circuit Court of Appeals and point out its fundamental errors.

F. Analyze the leading authorities on equitable assignment.

G. Distinguish the authorities relied on by the respondent and the Court below.

### A. Tests of Equitable Assignments.

(1) There can be no equitable assignment of a fund to come into existence unless (*a*) there was an intention to create an assignment; and (*b*) a *res* has been irrevocably appropriated the creation of which is a carrying out of the intention. Whether or not certain acts amount to the setting up of a *res* is in turn dependent upon the intention with which those acts are done.

*Hamer* vs. *Sidway* (1891), 124 N. Y., 538.

*In re Interboro Consolidated Corporation* (C. C. A. 2nd, 1923), 288 Fed., 334-349.

*Hopkinson* vs. *Forster*, L. R. 19, Eq. 74, where the Court said: "You can have no charge in Equity without an intent to charge. The letter on which you rely was not written with any intent to charge the fund; it was a mere letter of instructions to the bankers."

(2) There can be no equitable assignment unless the assignee knows of and consents to the setting up of the fund.

3 *Pomeroy Eq. Jurisprudence* (4th Ed. 1918), Section 1281 says:

> "Notice to the Creditor Assignee Essential.—Although, whenever a debtor, in the manner above described, makes to his creditor an equitable assignment of a specific fund or debt in the hands of or owing by a third person, the assent of such *third person* is not requisite to the effect of the transfer in equity, *yet the assignment, appropriation, direction, or order is not absolute, but may*

*be revoked by the debtor-assignor at any time before the creditor-assignee has been notified of it, and has expressly or impliedly assented thereto. In such a case notice to and assent by the creditor-assignee are essential to an absolute assignment.*" (And cases there cited.)

(3) There can be no equitable assignment or equitable charge unless the fund is taken in satisfaction of or as security for the obligation.

*Barnes* vs. *Alexander* (1914) 232 U. S., 117, 121;

*Spellman* vs. *Bankers' Trust Company* (C. C. A., 2nd 1925) 6 Fed (2nd), 799.

(4) If the fund or balance set up remains at the risk of the alleged assignor, there has been no equitable assignment.

*Tiernan* vs. *Jackson* (1831), 5 Peters 579, 594;

*Williams* vs. *Everett* (1811), 14 East, 581, 596;

*In re Interboro Consolidated Corporation*, 288 Fed., 334-345, quoting with approval *Story's Commentaries on Equity*, Section 1045, where it is said: "The true test whether an absolute appropriation is made out or not depends upon the point at whose risk the property is; and until the creditor has consented, the property will clearly be at the risk of the assignor or remitter."

(5) If the alleged assignor retains control over the fund or balance or may revoke his instructions with respect thereto, then there has been no equitable assignment.

F. Analyze the leading authorities on equitable assignment.

G. Distinguish the authorities relied on by the respondent and the Court below.

**A. Tests of Equitable Assignments.**

(1) There can be no equitable assignment of a fund to come into existence unless (*a*) there was an intention to create an assignment; and (*b*) a *res* has been irrevocably appropriated the creation of which is a carrying out of the intention. Whether or not certain acts amount to the setting up of a *res* is in turn dependent upon the intention with which those acts are done.

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(5) If the alleged assignor retains control over the fund or balance or may revoke his instructions with respect thereto, then there has been no equitable assignment.

In *Christmas* vs. *Russell* (1871), 14 Wall, 69, this Court said at p. 84:

> "An agreement to pay out of a particular fund, however clear in its terms, is not an equitable assignment; a covenant in the most solemn form has no greater effect. * * * *The assignor must not retain any control over the fund—any authority to collect, or any power of revocation. If he do, it is fatal to the claim of the assignee.*"

In *Cushings* vs. *Chapman* (C. C. Mo., 1902), 115 Fed. 237, the Court said at p. 239:

> "To constitute such an equitable assignment, there must be such an actual or constructive appropriation of the fund or subject matter 'as to confer a complete and present right on the party meant to be provided for, although the circumstances do not admit of its immediate existence'; *that, if the holder of the fund could retain control over it, with the power, sua sponte, on his part, to satisfy the promise in cash, it is fatal to an equitable assignment.* *Christmas* vs. *Russell*, 14 Wall 69, 20 L. Ed. 762; *Bank* vs. *Beal* (C. C.) 54 Fed. 577; *Badgerow* vs. *Trust Co.* (C. C.) 74 Fed. 925; *Ex parte Tremont Nat. Bank*, 24 Fed. Cas. 184; *Foss* vs. *Cobler*, 105 Iowa, 731, 75 N. W. 516; *Stearns* vs. *Insurance Co.*, 124 Mass. 63, 26 Am. Rep. 617; *Williams* vs. *Ingersoll*, 89 N. Y. 518; *Hicks* vs. *Brick Co.*, 94 Va. 746, 27 S. E. 596; *Hassack* vs. *Graham*, 20 Wash. 192, 55 Pac. 36."

See also *In re Stiger*, 202 Fed. 791 affirmed (C. C. A. 3rd, 1913), 209 Fed. 508; and *Spellman* vs. *Bankers' Trust Co.*, supra, at p. 800;

5 *Corpus Juris*, 913.

The following acts have been held *not* to indicate an intention to create an assignment:

(1) The mere advice to a bank of the drawing of a

draft in accordance with international banking practice does not indicate an intention equitably to assign any of the depositor's balance with the drawee.

*Eastman-Kodak Company* vs. *Park National Bank* (D. C. S. D. N. Y., 1916), 231 Fed., 320 (opinion by Learned Hand, D. J.), affirmed no opinion 247 Fed., 1002.

(2) The mere direction to pay a draft and charge it to the account of the depositor does not constitute an equitable assignment nor is there an equitable assignment even if the funds have been placed in the hands of the depositary as a *means* of satisfying the depositor's absolute obligation.

*National City Bank* vs. *Hotchkiss* (1913) 231 U. S., 50;

*Eastman-Kodak* vs. *Park National Bank* (1916), 231 Fed., 320, aff'd. 247 Fed., 1002;

3 *Pomeroy Eq. Jur.*, Sec. 1282, cited with approval in the *Interboro* case, *supra*, at 345, and citing *Cheney* vs. *Libbey*, 134 U. S., 68, 83;

*Aetna National Bank* vs. *Fourth National Bank* (1871), 46 N. Y., 82, 87.

(3) Even an agreement to pay a debt out of a designated fund does not give an equitable lien on the fund or operate as an equitable assignment thereof.

*Williams* vs. *Ingersoll* (1882), 89 N. Y., 508;
*Christmas* vs. *Russell* (1871), 14 Wall., 69.

(4) Mere book entries dividing a bank balance into two or three accounts, as a matter of convenience or in pursuance of a well established custom, do not evidence

an intention to assign a fund, and do not constitute an equitable assignment.

*In re Interboro Consolidated Corporation, supra;*

*Noyes* vs. *First National Bank* (1st Dept., 1917), 180 App. Div., 162, affirmed *on opinion below*, 224 N. Y., 542, and analyzed page 48, *infra;*

*Taussig* vs. *Carnegie Trust Co.* (1st Dept., 1913), 156 App. Div., 519, affirmed, no opinion, 213 N. Y., 627, and analyzed page 78, *infra;*

*Kuehne* vs. *Union Trust Company* (1903), 133 Mich., 602, analyzed page 79, *infra.*

**B. The Necessary Results of Respondent's Contentions.**

Respondent contended and the Court below held that there was an assignment *in favor of the draft holder* whose rights the respondent acquired by taking up the draft.

If the fund with the B. C. I. was intended to be and was equitably assigned to the draft holder, the following results would follow under the foregoing authorities:

(1) At the moment the fund was created, (if a "fund" was created), and even prior to the presentation of the inland draft, K. N. & K. was fully discharged despite the fact that Trinidad remained liable to the holder on its draft.

(2) At the moment the fund was set up, K. N. & K. lost all control over it and the debtor-creditor relationship between B. C. I. and K. N. & K. ceased.

(3) After the fund was set up, it was wholly at the

risk of the inland bank (or of the draft holder); that is, if the B. C. I. in the present case, or if in other cases any one of the hundreds of scattered foreign correspondents named in the list, became insolvent after the fund was set up and before the draft was presented, or for any reason failed or refused to pay the draft upon presentation, the loss would fall, not on K. N. & K., but on the inland banks which in fact did not choose the foreign correspondents or have any knowledge or means of knowledge of their solvency or responsibility.

(4) The various steps taken by or acquiesced in by K. N. & K. would have to be construed as necessarily taken to carry out a previous intention and obligation under the provisions of the Drawing Service to create and assign *in advance* a fund abroad, *despite the fact* (*a*) that those very same steps were taken in the simple case where K. N. & K. issued their own drafts without any such special contract, and (*b*) that such steps are taken by international bankers generally in pursuance of well established usage and custom existing for wholly different reasons and irrespective of any special promise.

*It will now be shown however, that no such results were intended or effectuated;* that K. N. & K. were not discharged until payment of the draft; that K. N. & K. at all times controlled the funds on deposit with B. C. I.; that the risk of loss in the event of the failure of B. C. I. was on K. N. & K. and not on Trinidad; and, finally, that the very steps here taken were the usual and ordinary steps taken in accordance with general international practice and custom, and, indeed, the same steps taken by K. N. & K. in protecting drafts drawn by themselves although no agreement in the nature of the Drawing Service was entered into with respect to such drafts.

As a result, there is no basis for respondent's con-

tention that funds were equitably assigned in favor of Trinidad or the holder of the draft.

### C. Neither the Provisions of the Drawing Service Nor the Acts Done in the Performance of K. N. & K.'s Obligations Were Intended to or Did Constitute an Equitable Assignment.

Having now stated the basic legal principles involved and the necessary results of respondent's contentions, the contract of the parties and the acts done pursuant thereto will be examined and it will be shown that there was no equitable assignment.

#### 1. The provisions of the Drawing Service, and the forms provided for use therewith, do not disclose any intention that any "fund" should be created in advance or assigned for the payment of the draft drawn by Trinidad on the B. C. I.

In construing the provisions of the Drawing Service contract, the Court must consider all of the provisions together in order to determine the purpose and effect of the whole rather than give undue emphasis to isolated words or phrases without their relation to the other provisions of the contract.

The primary purpose underlying the Drawing Service contract and the results which the parties thereto hoped to accomplish is best evidenced by the preliminary statement in the List of Foreign Correspondents (Claimant's Ex. 1, fol. 418). The opening paragraph states:

> "Inasmuch as the maintenance of a Foreign Department *involving the carrying of balances abroad*, etc., is *undesirable* from the standpoint of a majority of the inland banks, we have aimed for

> many years to supply this want by *extending* to our correspondents the privilege of using *our world-wide facilities* for carrying on a foreign exchange business."

It was thus the basic purpose of the Drawing Service to substitute *K. N. & K.'s foreign credit* for the necessity of the inland banks having balances abroad; the latter was declared to be "undesirable." Further, "extending" to the inland correspondents the privilege of using the world-wide facilities of *K. N. & K.* for carrying on a foreign exchange business simply meant that K. N. & K. would make available for the payment of the inland bank drafts *K. N. & K.'s own balances* or credit in foreign countries which K. N. & K. would direct to be charged upon the "honoring" of the draft (Claimant's Exhibit 6D, fol. 499), when presented. The relationship contemplated did *not* involve the setting up abroad of a credit in favor of the inland bank or of the draft holder in advance of the presentation of the draft or, for that matter, at any time. *The scheme here devised was, in its essence, a convenient substitute for the purchase by the inland bank of K. N. & K.'s own drafts upon which K. N. & K. would remain liable despite the failure of their foreign correspondent.*

*Effect of direction of Trinidad to K. N. & K. to protect draft on presentation.*

It is submitted that the most important single document in the chain comprising the contract between the parties is the form of advice *prepared by K. N. & K.* and sent by Trinidad (and of course by every other inland bank using the service each day) to K. N. & K. to instruct K. N. & K. what they should do. This advice (Claimant's Ex. 4, fol. 482), after stating that Trinidad had sold the draft in pursuance of the Drawing Service, added that Trinidad:

> "shall thank you to *protect* same *upon presentation.*"

This direction clearly negatives any idea that K. N. & K. was to create a fund in advance or could by so doing discharge their obligation. The phrase "to protect a draft upon presentation" has a well recognized meaning. It is a personal general obligation to see that the draft is *paid*. That is the meaning which business men, the courts and lexicographers have uniformly given to it. Thus in *Wabash St. L. & Pac. Ry. Co.* vs. *Ham* (1885), 114 U. S., 587, a consolidation agreement provided that the bonds and debts therein specified of the former companies should "be *protected* by the said consolidated company." It was urged that under this provision a lien had been created in favor of the bonds and debts of the former companies upon the assets of the consolidated company. This Court held to the contrary, saying through Mr. Justice Gray, at page 596:

> "The agreement 'to protect' referring to the time of payment, and 'the true meaning and effect' of the equipment bonds having been to create only a personal and unsecured debt of one of the former companies, *the words 'shall be protected' must have the same meaning which they ordinarily have in promises of men of business 'to protect' drafts or other debts not made or contracted by themselves, that is to say, a personal obligation to see that they are paid at maturity.*"

That the foregoing definition has been accepted appears from *Webster's New International Dictionary*, 1924, where the above case is referred to as the basis of the meaning of the word "protect" in commerce and finance:

> "4. Com. & Finance. To see that (a note, draft or other obligation) is paid or satisfied at maturity (114 U. S., 587); as the Consolidated Company

agreed to *protect* the bonds of the individual companies."

And in *Funk & Wagnall's New Standard Dictionary*, the following definition of "protect" is found:

"4. *Finance.* To guarantee payment of or satisfy at maturity, as bonds."

*Robbins* vs. *Robinson* (1896), 176 Pa., 341, 346:

"To 'protect a bill' for the seller means in any reasonable business construction to be answerable for its *payment* * * *."

*The instructions of K. N. & K. to its correspondent—B. C. I.*

That this was the meaning understood by K. N. & K. is confirmed by the language used in the advices sent by K. N. & K. to the B. C. I. (Claimant's Exhibits 6 and 6D, fols. 487, 469). In the advice sent to the main Genoa office of the B. C. I., K. N. & K. requested the B. C. I. to

"Please *protect* to the debit of our account* the drafts as per particulars on the attached copies * * *."

And in the advice sent to the specific branch of the B. C. I. on which the draft in question was drawn (Claimant's 6D, fol. 469), K. N. & K. requested

"Please *honor* the above listed drafts charging same to our account with Banca Comm. Italiana Genoa."

The term to "honor" a draft also has of course a well

*The direction to "protect" to the "debit of our account" was used in the same sense in the advice appearing in the case of *Eastman Kodak Company* vs. *Park National Bank*, 231 Fed., 321, affirmed (C. C. A., 2d), 247 Fed., 1002.

defined meaning. Thus in 30 *Corpus Juris*, 457, it is stated, quoting numerous cases, that "honor" as a verb means:

> "also to accept a bill of exchange, or to *pay* a note, check, or accepted bill, *at maturity* and according to its tenor."

Nothing is said about the transfer of a credit for the benefit of either the Trinidad bank or the holder of the draft. Nothing is said as to the creation of a fund in advance. The instructions are to "protect" and to "honor" the drafts presented.* If the intention had been that K. N. & K. should *in advance* appropriate a fund for the payment of a draft, then it would have been easy to provide simply that K. N. & K. should set up a credit for Trinidad so that when the draft was presented Trinidad would have had a credit *of its own* on the B. C. I.'s books to which its draft could be charged. Transactions of this kind are accomplished daily in great number by the ordinary cable or mail transfers (See *Legniti* and *Gravenhorst* cases, *infra*). If this had been the intention, the lengthy and special provisions of the Drawing Service contract would have been unnecessary. But this was not at all the intention of the parties or the scheme of the Drawing Service. *The underlying purpose of the Service was that the draft should be treated just like a draft K. N. & K. itself had drawn; and just as K. N. & K. would direct the B. C. I. to "honor" or "protect" their own drafts, and would, of course, have a balance there at the time of presentation to meet them, so the scheme was to "protect" the payment of the inland bank's draft by K. N. & K. having a balance with the B. C. I. to which account the draft could be charged when it had been presented and paid.* Such a system required a balance in

*As said in *Hopkinson vs. Forster*, L. R. 19, Eq. 74, supra, "The letter on which you rely was not written with any intent to charge the fund; it was a mere letter of instructions to the bankers."

the form of a K. N. & K. credit *at the moment of presentation and not before.*

Thus only could the inland bank achieve the result which it desired. Only in that way did K. N. & K. remain under an absolute contractual obligation to see to it that the draft was paid upon presentation—to protect it—and remain undischarged until such payment. *Payment abroad is what Trinidad desired. It had drawn a draft upon a bank which it did not know and which K. N. & K. did know. It had relied solely upon K. N. & K. themselves. It wished to look to K. N. & K. in the event that the draft was not paid and it did not wish to trouble itself with foreign credits. That was deemed "undesirable."*

Accordingly K. N. & K. undertook by the general terms of the Drawing Service itself that upon receipt of the advice of the drawing of the draft by Trinidad (referred to above) and the receipt of the consideration in American dollars:

> "We shall promptly forward our advice of the same and provide the drawee *with funds sufficient* for the payment of the draft abroad by a transfer of credit from our balance, or otherwise" (fol. 422).

**Nature of Obligation to Provide Drawee With "Funds Sufficient for the Payment of the Draft."**

The obligation to provide "sufficient funds" was the same obligation as that discussed in *Beecher* vs. *Cosmopolitan Trust Co.*, 239 Mass., 48, analyzed at p. 71, *infra*, where the Court used those very words. But in that case there was no intimation that such funds were to be irrevocably appropriated in advance of the presentation of the draft. And in *Erb* vs. *Banco di Napoli*,

243 N. Y., 45, analyzed at p. 50, *infra*, the Court said that the Italian Government "had *provided funds* to meet its obligations" and yet the Court held there was no trust in favor of the coupon holders.

There was *no* undertaking by K. N. & K. to provide the foreign bank with "*a fund*" for the payment of the draft. K. N. & K.'s only obligation was to provide the drawee with "*sufficient funds*" for the draft's payment. This, in the light of all the documents furnished in the Service meant simply that K. N. & K. undertook to notify the foreign bank that the draft had been drawn and further undertook to see to it that the foreign bank would pay the draft when it was presented. Such payment, upon the presentation of the draft, was to be accomplished either by a transfer from K. N. & K.'s balance—that is by a debit to the K. N. & K. account—or was to be accomplished "otherwise," which, of course, meant that in those cases where K. N. & K. had no foreign balance in the particular drawee bank, arrangement would somehow be made by K. N. & K. for having the draft paid—for example, by directing a foreign bank with which they did have a balance to arrange for the payment of the draft when presented to the drawee, i.e. to "protect" the draft.

It is apparent therefore that under the Drawing Service and the forms used in connection therewith, which together evidenced the contract of the parties, *there was no intention that any fund should in advance be assigned or appropriated to the payment of the draft.* The absence of any such intention *is of itself fatal* to the contention now advanced (in order to obtain a preference over other creditors) that any portion of the balances of K. N. & K. at the time of the filing of the petition in bankruptcy had been equitably assigned.

2. THE ACTS DONE BY K. N. & K. AND BY THE B. C. I. IN THE PERFORMANCE OF K. N. & K.'S OBLIGATION UNDER THE DRAWING SERVICE, INCLUDING THE BOOKKEEPING ENTRIES MADE BY THE B. C. I. PURSUANT TO A WELL ESTABLISHED INTERNATIONAL BANKING CUSTOM, ARE NO EVIDENCE OF AN INTENTION TO ASSIGN OR APPROPRIATE A FUND. THIS IS PARTICULARLY SO, INASMUCH AS K. N. & K. AT ALL TIMES RETAINED CONTROL OF THEIR BALANCE AND HAD THE RIGHT TO CANCEL ADVICES, AND THUS REMAINED THE CREDITOR OF B. C. I.

It has just been shown that the contract of the parties did not contemplate an assignment or appropriation of a specific fund abroad. It will now be shown that the *acts* of the parties—their construction of their obligations *ante litem motam*—do not evidence an equitable assignment.

On receipt of the Trinidad bank's check in American dollars (Claimant's Exhibit 3, fol. 481) together with the advice from Trinidad (Claimant's Exhibit 4, fol. 482) K. N. & K. promptly sent an advice to the B. C. I., upon which Trinidad had drawn its draft. Such advice was composed of a statement to the main branch of the B. C. I. at Genoa (Claimant's Exhibit 6, fol. 487) containing a statement of all drafts drawn on the B. C. I. and its branches for a given period and instructing the B. C. I. to "please protect to the debit of our account the drafts as per particulars on the attached copies." The "attached copies" were copies of advices which K. N. & K. had sent to each of the individual branches of the B. C. I. upon which drafts had been drawn by them or under their protection (see Claimant's Exhibits 6A-6E, fol. 490, *et seq*). One of such copies (Claimant's Exhibit 6D, fol. 499) was addressed to the Sassari branch of the B. C. I. and included an advice of the draft here in question drawn by the Trinidad bank. Such advice requested the B. C. I. to "please *honor* the above listed

drafts charging same to our account with Banca Comm. Italiana, Genoa."

It is important to note that included in the advices sent to the B. C. I. by K. N. & K., were drafts drawn not only by inland bank correspondents of K. N. & K. (such as the Trinidad bank in this case), but also by "ourselves"—K. N. & K. (See, for example, Claimant's Exhibits 6A, fol. 490 and 6E, fol. 502). *In other words, K. N. & K. took exactly the same steps to protect that drafts drawn by themselves as were taken to protect drafts drawn by their inland correspondents under the Drawing Service.* It will also be shown that the B. C. I. on receipt of K. N. & K.'s advice acted in the same manner with respect to K. N. & K.'s own drafts and the inland bank drafts. *Therefore irrespective of other arguments, if no equitable assignment was contemplated or effected as a result of the issuance of K. N. & K.'s own drafts, none was contemplated or effected as a result of the issuance of the inland bank's drafts including the Trinidad Bank draft in this case.*

**The Debiting by B. C. I.**

Upon the receipt of the advice, the B. C. I. charged the amount of all the drafts, both those issued by various inland banks and those issued by K. N. & K. themselves, to the account which K. N. & K. maintained with the Italian Bank, and

> "simultaneously credited on its books an account termed 'drafts payable' in which account were also credited amounts of drafts advised to the said Banca Commerciale Italiana for payment by other depositors or clients of the Banca Commerciale Italiana in addition to the bankrupts" (fol. 92).

The following facts are to be noted:

(1) That K. N. & K. gave no directions to the B. C. I., to set up a fund which should be irrevocably appropriated to the payment of its own and of the inland drafts, but simply directed them to "protect" the drafts to the debit of their account and to "honor" the drafts, charging the same to their account.* *K. N. & K. simply acquiesced in the established banking practice of debiting which had an entirely different purpose.*

(2) That while K. N. & K.'s account in the B. C. I. was debited with the aggregate of all the drafts (*a*) no *direction* was given to set up in advance an account either in favor of the Trinidad Bank or in favor of the draft holder, which of course, is what ordinarily is done when a credit is established in favor of somebody by a cable transmission or otherwise; and (*b*) no account *was* ever set up in favor of the Trinidad Bank or of the draft holder.

(3) On the contrary all the drafts drawn by all of the depositors of B. C. I. were credited in an omnibus Drafts Payable Account, and, as will be shown, the credit in the Drafts Payable Account "is entered in a folio under the name of the bank *whose account has been charged*" (fol. 350), in this case, under the name of K. N. & K.

Yet, it is from these very acts and circumstances that the respondent urges that there must be found an intention equitably to assign a specific fund for the payment of the draft drawn by Trinidad.

Not only is no such intention found in the mere acts themselves, *but on the contrary*, the record shows affirmatively and without contradiction that the entries were made in accordance with well recognized international banking practices existing for wholly different reasons.

*As a means of reimbursement—*National City Bank* vs. *Hotchkiss*, 231 U. S., 50, analyzed *infra*, p. 85.)

**Testimony of Dawson as to Reasons for Existence of "Drafts Payable Account."**

**Its Creation Independent of Drawing Service Contract.**

The reasons for the existence of the international banking custom, as appears from the *uncontradicted testimony of the expert witness Dawson*, about to be analyzed, are two-fold:

(*a*) That it was a convenient method of indicating to the drawee banker what his commitments were likely to be in the immediate future and thus enabled him to have liquid and available for immediate use enough capital to meet those commitments;

(*b*) That while the banker paid interest to his depositor on the balance in the latter's general account, no interest was paid on the amount of his funds credited to the Drafts Payable Account, and that the use of this latter balance without the payment of interest thereon between the time of its credit to the Drafts Payable Account and the presentation of the draft drawn by the depositor or under his protection constitued the foreign bank's compensation for its services in meeting the draft.

Ralph Dawson, Vice-President of the Guaranty Trust Company of New York, has had extensive experience in international banking for over 25 years (fol. 345), and has had experience in all branches of the foreign exchange business (fol. 340 *et seq.*). He is familiar with and has handled foreign exchange transactions, both in which the New York banks drew their own drafts upon foreign correspondents (fol. 345) and also involving the "protection of drafts by New York banks, bankers or trust companies on behalf of inland banks" (fol. 346).

At fol. 350 he testified:

> "The Witness.—The practice is to charge the current account of the client with the sum of money and carry it over into another account which is known on the ledgers of most banks as 'unpresented drafts drawn,' *where it is entered in a folio under the name of the bank whose account has been charged.*" (The "unpresented drafts drawn" account is the "Drafts Payable Account" referred to throughout this brief).

In other words, although B. C. I. debited K. N. & K.'s general account and credited the unpresented drafts payable account, the credit was entered in a folio, *not* under the name of the Trinidad Bank or the draft holder, *but under the name of K. N. & K.*, thereby indicating that the balance still belonged to K. N. & K. and was subject to their control.

The reasons for the existence of this custom at the present time were stated by Mr. Dawson to be as follows (fol. 357):

> "Q. How has that practice developed in modern times? A. Well, the practice has hung on in modern times, like a great many other practices, and has been availed of *as a means frequently of compensating a banker* for an account that would otherwise be troublesome and a loss. You have many accounts frequently that are active, which on bare balances in current accounts, are a lot of trouble, and a loss in handling that would not be worth while, but *there is always a non-interest bearing float that compensates you for the trouble you take.*
>
> Q. So that in reality *there are two reasons, are there not, generally assigned, namely, to put the drawee bank or banker in a position to meet the drafts which have been advised, and to enable him to use that fund as he may without paying interest thereon to the person who has the account?* A. *That is right.*"

And at fol. 370:

> "Q. That is, knowing how much the advised drafts are, you know how much money you have to keep as ready cash? A. Yes.
>
> Q. And you determine the amount of drafts which are to come from your general omnibus Drafts Payable Account? A. Yes.
>
> Q. That is, any day, looking at your Drafts Payable Account, you know how many outstanding advised drafts there are, how much that amounts to, and therefore, you know how much available cash you have to have in order to meet that draft? A. Yes."

And at fol. 373:

> "The Master.—And under the present system does the bank have the use of that money until the draft is presented for payment?
>
> The Witness.—Yes.
>
> By Mr. Goldmark:
>
> Q. They can lend it on the street? A. Yes.
>
> Q. That is, they could lend a sum equivalent to some one on the street, so that, at any moment, if the number of drafts which had been advised, which came in on a particular day, was more than the average number that came in on another day, you would always know at the beginning of the day how much money you needed from your Drafts Payable Account to meet outstanding drafts? A. Yes."

In addition to explaining the present practices and the reasons underlying them, Mr. Dawson testified as to the *origin of these practices*. He stated, in substance, that in the past when there were no Federal reserve banks, banks of rediscount or methods of suddenly raising cash, an international banker on being advised that his depositors had drawn drafts on him, would convert some of *his own* non-liquid assets into cash and hold the cash

ready to meet the obligation, namely, the payment of the drafts which his depositor had drawn (fol. 356). The respondent sought below to find in Mr. Dawson's testimony just referred to proof of an intention to assign a particular fund for the payment of a draft not yet presented.

The testimony only showed that in the times referred to by Mr. Dawson, before the existence of the present elaborate credit system, bankers found it necessary to convert enough *of their own assets* into cash so that they could conveniently meet their expected obligations. The cash so set aside was not however irrevocably appropriated by them to the expected obligations but was set aside, according to Mr. Dawson's testimony, purely as a matter of convenience (fol. 356).

**K. N. & K. at all Times Remained the Owner of and in Control of the Balance in the Drafts Payable Account for They Could Always Have Cancelled the Draft.**

It has been shown at page 17 *supra*, that if K. N. & K. retained control of their foreign balance, that balance cannot be deemed to have been irrevocably appropriated or equitably assigned to the respondent. That they *did* at all times retain such control is shown by the uncontradicted testimony of Dawson.

At folio 350 *et seq.* he testified:

> "Q. Is there also a general practice or custom with respect to the cancellation of advices after their receipt by the foreign bank and prior to the presentation of the draft for payment? * * * A. Yes, there is a custom.
>
> Q. What is that custom? * * * A. I take it the question means that the drawer bank wants to cancel a draft that has already been drawn and advised.

Q. Precisely? A. A communication of the fact of cancellation by any means he can avail himself of, cable, letter or anything else. Upon receipt by the drawee bank that such draft has been cancelled, a reversal entry is passed, taking the amount of such cancelled draft from the unpresented draft ledger and crediting it back into the current account."

He further testified (fol. 353):

"Q. And does that same custom prevail in the case of drafts drawn by inland banks, where the advice is by the New York bank? * * * A. Yes, because the foreign bank, the drawee bank, does not know the party who is drawing. * * *

Q. Is such cancellation ordinarily and customarily effected without assigning any reason? * * * A. The drawee bank acts entirely on the orders *of its client*.

Q. Which is the bank— A. Which is the bank that has the account on its books." (In this case K. N. & K.)

Despite the clarity of Mr. Dawson's testimony to the effect that "the drawee bank acts entirely on the orders of its client"—in the present case K. N. & K. and not Trinidad—the respondent urged below that Mr. Dawson's testimony showed that K. N. & K. could only cancel the draft where the inland bank had requested them to do so. The respondent rested its contention entirely upon Mr. Dawson's statement at folio 351 just quoted that the foreign bank would cancel an advice where "the *drawer* bank wants to cancel a draft that had already been drawn and advised."

It is clear, however, that at that stage of the examination no mention had yet been made of drafts drawn by one bank under the protection of another, as in the present case. Only the usual situation of the drawing of a draft on a foreign bank by the depositor himself was then being considered. Mr. Dawson's reply was

simply to the effect that in that usual situation the foreign bank would at all times cancel the advice at the request of the "drawer"—"drawer", under the circumstances then being considered, meaning the foreign bank's depositor.

The respondent disregarded in its argument below the subsequent testimony of Mr. Dawson in reply to questions by the respondent's own attorney where Mr. Dawson made it entirely clear that the foreign bank always accepted the instructions of its client-depositor whether that client had advised its own draft or the draft of an inland bank. Mr. Dawson's testimony at folio 368 is as follows:

> "Q. You made an answer to Mr. Goldmark to the effect that these cancellations were effected upon notification from the drawer, didn't you? A. No, sir, *from the client.*
>
> Q. Then I may have misunderstood you. A. *When the question was asked there was no question of a third party.*
>
> Q You mean the person who drew the draft, when you say client? A. *No, sir, I mean the name that is on the books of the drawee bank is the client or the owner of the funds.*
>
> By Mr. Goldmark:
>
> Q. *You mean the person who has the account in the bank?* A. *Yes, sir.*
>
> Q. *They cancel the advice at his request whether he is the drawer of the draft or whether he is the person who advised the draft drawn by somebody else?* A. *Yes, sir; at his order they will cancel the draft.*"

**The Forms Used for Cancellation.**

The fact that K. N. & K. at all times remained in control of their foreign balances and cancelled advised drafts at their will is further supported by the fact that

K. N. & K. had regular printed forms which they used to accomplish this result (Trustee's Exhibits 3 and 4, page 192). Those forms contained no reference to the fact that the cancellation was pursuant to the request of the inland drawer bank and very apparently the foreign drawee bank was not interested in that information. The foreign bank, the B. C. I., honored K. N. & K.'s instructions because it considered itself obligated only to K. N. & K. and recognized no obligation either to Trinidad or to the draft holder. It was not the practice in requesting the cancellation of advices of "protected" drafts to advise the B. C. I. that such cancellation was at the request of Trinidad or any inland bank (fol. 222). As Mr. Dawson clearly stated at folio 368 already quoted, the foreign bank only recognized the instructions of its own depositor whether that depositor was itself the drawer of the draft or whether the depositor merely advised and requested the protection of a draft drawn by somebody else.

In the light of the foregoing testimony there can be no doubt that K. N. & K. at all times remained in full control of all their balances abroad including the portions thereof credited to the Unpaid Drafts Account.

**Other Evidence Confirming Dawson's Testimony as to Custom.**

The existence of the international banking practice to which Mr. Dawson testified is also confirmed by the testimony of Mr. Schulze (fol. 327). On this phase of the question it is important also to note Mr. Schulze's testimony (fols. 400 to 402), that in cases where *dollar* drafts were drawn on the B. C. I. (as distinguished from drafts drawn in lire as in the case at bar), the amount thereof was not charged against K. N. & K.'s general account on receipt of the advice and was not credited to the

Drafts Payable Account, and that, therefore, inasmuch as the B. C. I. had the use of no credit without the payment of interest pending the presentation of the draft, it received a commission for honoring these dollar drafts. The application of the general custom testified to by Mr. Dawson, under which the B. C. I. looked only to its customer, K. N. & K., for instructions as to cancellation and recognized K. N. & K.'s sole control over their balances both in their general account and in the Drafts Payable Account, is confirmed by the testimony of Mr. Schulze (fols. 216-219) and 234-238). The absolute control of K. N. & K. over their balance with the B. C. I. has been clearly demonstrated.

Mr. Dawson's testimony is also supported by the facts *stipulated* at fol. 378 to the effect that the B. C. I. cancelled drafts drawn either by K. N. & K. or under their protection and that

> "This was done *without knowledge* on the part of the B. C. I. as to whether such draft or drafts were in the possession of the bankrupts, the drawer banks or third persons."

**D. The Conclusions from the Foregoing Facts Show that the Tests of the Existence of Equitable Assignment Have Not Been Met.**

The foregoing facts* establish the following propositions:

(1) There was no intention on the part of K. N. & K. or the Trinidad bank to assign any funds abroad, K. N. & K.'s sole obligation being to have the draft paid *at presentation*, as in the case of drafts drawn by K. N. & K. themselves, and thus see to it that Trinidad's obligation to its customer and the payee was performed. K.

*The errors of the Court below in interpreting the testimony are considered at page 42, *infra*.

N. & K. agreed to furnish sufficient funds as a *means* of enabling them to perform their obligation.

(2) *K. N. & K. did not direct B. C. I. to set up any particular fund* but simply directed the debiting of the drafts to their general account upon presentation. And *no fund was in fact set up* in favor of Trinidad or the draft holder or irrevocably appropriated abroad. The credit to the omnibus Drafts Payable Account was made, not in pursuance of K. N. & K.'s obligation under the Drawing Service, but pursuant to the well established international banking custom. The same practice was pursued with respect to drafts drawn by K. N. & K. themselves, although their issuance was *not* governed by the terms and conditions of the Drawing Service. This custom exists for reasons entirely independent of a desire irrevocably to create a fund.

(3) The final "debit" and the final "charging" were of course to take place when the draft was "protected" or "honored" by the B. C. I. and not before. Because of the reasons and *subject to the control* just explained K. N. & K. acquiesced in the general international banking practice of debiting their account and crediting Drafts Payable Account pending the presentation of the draft.

(4) The Trinidad bank did not agree to look alone to the fund abroad for the payment of the draft drawn by it, but desired and procured K. N. & K.'s general obligation "to protect" that draft when presented. *Does the respondent seriously argue that the intention underlying the Drawing Service as agreed to by the parties was that the large and small banks scattered throughout this country, which had no knowledge of foreign banks and bankers, were paying over their money to K. N. &*

*K., relying on the credit, solvency and responsibility of foreign correspondents in scattered communities throughout Europe, wholly unknown to them and chosen by K. N. & K.?* What the inland banks wanted was that their drafts drawn upon foreign bankers with whom they had no relations whatever and of whom they knew nothing, be honored. They did not want funds set up in innumerable places throughout Europe which would be there at their risk, awaiting the presentation of the drafts. If the reverse were true, every bank throughout the country which availed itself of the service of K. N. & K. or other New York bankers, affording a like service, would have to look solely to the foreign bank, and in the event of its failure or refusal to pay, loss would not fall on K. N. & K. but on the inland banks. Such a conclusion would be inconsistent with the stated purposes of the Drawing Service where the maintenance of foreign balances by the inland banks was said to be "undesirable." *K. N. & K. having chosen the correspondents abroad and being in touch with foreign banking centers could well accept the same risk of loss on "protected" drafts that they accepted in drawing their own drafts on the very same correspondents.*

(5) The balance with the B. C. I. was at all times at the risk of K. N. & K., inasmuch as they had assumed an absolute obligation to have the drafts paid on presentation, from which obligation they would not have been relieved by the failure of the B. C. I., with the consequent loss of their balance.

(6) It appears from the undisputed testimony of Mr. Dawson and Mr. Schulze and from the stipulations in the record (fol. 378) just referred to that both that portion of the balance standing on K. N. & K.'s credit on the books of B. C. I. and that portion credited in the

Drafts Payable Account, was at all times at the absolute control and disposition of K. N. & K. and that the B. C. I. looked only to K. N. & K. for instructions as to the disposition of both balances. That is, K. N. & K. always remained the creditor of B. C. I.

### E. The Errors of the Court Below.

The essence and underlying premise upon which the Circuit Court's conclusion rests is found in the first three paragraphs of its opinion (fols. 749-754) and particularly in the very first paragraph. *And that premise is erroneous.*

The Court's entire opinion rests upon its initial statement that (fol. 750):

> "Performance once executed was irrevocable, because there was no intimation of any right to revoke it, and because the continued liability of the bankrupts was not an equivalent of performance, as the event proved. An obligee is not exposed to the renewed hazard of performance, once the obligor has performed, nor may the obligor at his whim undo that which he once did in satisfaction of his promise. * * *"

The Court has in the statement quoted assumed the very conclusion which it worked around to again at the end of its opinion. Of course, if the crediting of the Drafts Payable Account abroad constituted "performance" by K. N. & K., the credit was irrevocable. But there is nothing to show that that was intended to be performance. The Court's construction of the words in the instructions from Trinidad to K. N. & K. to "protect on presentation" is contrary to the universally accepted meaning of the banking terms. Again the only directions to B. C. I. were to "protect" and to "honor" to the debit of K. N. & K.'s account. All of Dawson's testi-

mony as to the custom of creating the Drafts Payable Account abroad irrespective of any special contract, as to the reasons for that custom and as to K. N. & K.'s retention of control over the foreign balance even after the credit to the Drafts Payable Account, was dismissed by the Court at folio 766 as follows:

> "There remains the question of custom. The evidence went no further than to show a practice of reversing the credits when the draft was cancelled. That was natural enough, but it is quite another thing to do so while the draft is outstanding."

*The Court is simply and clearly in error. The evidence —the uncontradicted evidence—did go further.* The testimony of Mr. Dawson at folio 368, already quoted at page 37, *supra*, clearly shows that the foreign bank looked *only* to its customer for instructions relative to cancelling drafts and from the stipulation at folio 378, it appears that "this was done without knowledge on the part of the B. C. I. as to whether such draft or drafts were in the possession of the bankrupts, the drawer banks, or third persons." It further appears that B. C. I. cancelled drafts without being informed that the cancellation was made upon request of Trinidad (fol. 222). It is true that the Trustee conceded, folio 379, that K. N. & K. only *did* cancel advices when instructed by the inland bank to do so. But the foreign bank knew nothing of this; it looked only to K. N. & K.; the latter retained full control despite the Drafts Payable Account. That K. N. & K. never did cancel except on the inland bank's instructions, does not bear on the question of their control over the foreign balance; it simply indicates that K. N. & K. having been paid to protect a draft, never found it necessary to cancel a draft unless advised to do so. It does not indicate that they *could* not have done so.

Further evidence that the credit to the Drafts Payable Account was not intended as "performance" is found in the stipulation, at folio 383 that the B. C. I. took the same action with respect to drafts drawn directly by K. N. & K. as it did with respect to those drawn by inland banks under the Drawing Service and protected by K. N. & K. *The Court below entirely disregarded this fact.* K. N. & K.'s drafts were drawn pursuant to no special contract like the Drawing Service. K. N. & K. remained liable on them as drawers until they were paid. No "performance" other than payment was conceivably contracted for. Yet credits to the Drafts Payable Account were made for those drafts also.

While it overlooked the facts concerning the bankrupts' own drafts in this case, in its opinion in *In re Zimmerman* vs. *Forshay, Ex parte Gray,* 14 Fed. (2d) 527, the Court was presented with a case involving just that situation—a draft drawn by the bankrupts without a special contract, advised abroad, and the amount thereof credited to a Drafts Payable Account. *The Court in that case, in order to remain consistent with its holding in the present case, was forced to this remarkable position:*

> "Although it is not so proved, we think that we must assume that when on receipt of the advice, the drawee made the entries upon its books, it did so in pursuance of a pre-existing agreement with the drawers. At any rate it is proved that the drawee advised the drawers of what it had done, and there is no evidence that the drawers protested."

That is, the Court undertook to indulge in an assumption unsupported by any evidence, and directly contrary to the theory of the Drafts Payable Account fully explained *by the uncontradicted testimony* of the expert Dawson.

To support its initial assumption that the bookkeeping entries abroad constitued "performance" by K. N. & K. the Court argued, at folio 752 that:

> "If they (K. N. & K.) had meant to become guarantors, the relation and the word were familiar enough, and it seems to us incredible that they should not have said so more unequivocally."

The Court is confused. The Trustee has not argued that K. N. & K. were guarantors—that they obligated themselves to perform the obligation of another. K. N. & K.'s contract was *not* with the draft holder to have the draft paid if the inland bank drawer did not pay it. The draft holder knew nothing of K. N. & K.'s existence. Their name did *not* appear on the draft. K N. & K.'s obligation was single, direct and primary—an obligation to the drawer inland bank to see that the latter's draft was paid. That is no guaranty; it is a primary obligation which could not be discharged by the creation of a fund abroad. K. N. & K.'s obligation was to have the draft *paid; not to establish a credit for the drawer.*

**Summary.**

A. When the Circuit Court of Appeals held that the advice of the draft followed by the crediting of the amount in the Drafts Payable Account constituted "performance" by K. N. & K. and an irrevocable appropriation of the amount of the credit to the performance of the contract, *the Court was erroneously giving to a coincidence the effect of a contracted for result*—a coincidence because the same thing happened (1) in cases where K. N. & K. had not entered into a contract like the Drawing Service, i. e., where they drew their own drafts; and (2) in cases of other drafts than those drawn or protected by K. N. & K., i. e., in the *Zimmerman & Forshay* case. That the credit to the Drafts Payable

Account had nothing whatever to do with the Drawing Service Agreement between K. N. & K. and Trinidad Bank is further proven by the fact that there is nothing to show that the drawee bank ever knew of the existence of the Drawing Service contract, or that K. N. & K. had given it any instructions to charge their account in order to perform K. N. & K.'s obligation.

B. The *second* underlying error of the Court below is its failure to give effect to the universally accepted meaning of the terms "protect" and "honor" as used in banking transactions and as used in the documents here under consideration.

C. The *third* underlying error of the Court below is its failure to accept and give effect to *the uncontradicted testimony* of Dawson as to the history and purpose of the Drafts Payable Account. The Court failed, also, to give effect to the uncontradicted testimony that it was the universal practice and custom for the foreign bank to always recognize the instructions of its customer to cancel advices prior to the presentation of the draft and for the foreign bank to consider that the relation of debtor and creditor continued to exist between it and its depositor until the draft had actually been presented and paid, despite the advice of the draft and the credit into the Drafts Payable Account. **No stronger evidence of the existence and recognition of the custom and of the fact that the crediting of the Drafts Payable Account was not an irrevocable appropriation can be presented than the fact that both in the present case and in the Zimmerman & Forshay case, the instructions given by the two Receivers were honored by the foreign banks.** The drafts theretofore advised were cancelled and the amounts theretofore credited to the Drafts Payable Account were recredited to

the general account of the bankrupt and the entire balance remitted to the Receiver. *In the light of these facts, this Court should pause before it fails to give effect to the established practice of banks, the reasons for which are so clearly set forth in Mr. Dawson's testimony.*

The fourth error of the Court below was its conclusion that there had been an equitable assignment in favor of the *payee or subsequent holder of the draft*, as distinguished from the Trinidad Bank, the drawer. The Court granted Trinidad's reclamation petition on the theory that the Trinidad bank, upon taking up the draft, had acquired the holder's rights. That this was the basis of the Court's conclusion appears most clearly from its opinion in the case of *In re Gubelman, Ex parte Muntean* (C. C. A. 2d 1926), 13 Fed. (2d), 730, already referred to, where the Court, in distinguishing the present case, said at page 732:

> "We decided the drawer, having taken up a draft drawn under the same 'service contract', stood in the position of an equitable assignee. It is true that this depended upon the drawer's subrogation to the holder's right, but the facts were not the same as here."

The extent of the respondent's rights is therefore limited strictly to the extent of the rights of the holder of the draft. The Court overlooked the elementary principle that *there can be no equitable assignment or irrevocable appropriation before the assignee has been notified of the assignment and has expressly or impliedly assented thereto.** As has already been shown, there is no evidence or claim that the holder of the draft (upon which the name of K. N. & K. nowhere appeared) at any time had any knowledge of the provisions of the Drawing Service, of the creation or existence of the Drafts Pay-

**Pomeroy Eq. Jurisprudence*, Section 1281, *note*.

able Account, or indeed of the existence of K. N. & K. themselves.

The fifth error of the Court below was its failing to hold that, since the foreign balance remained at all times subject to the absolute and sole control of K. N. & K., the balance passed to the Trustee under Section 70 (3) and (5) of the Bankruptcy Act as "property which prior to the filing of the petition he (the bankrupt) could by any means have transferred * * *."

## F. Leading Cases on Equitable Assignments and the Tests as to Their Creation.

### The Noyes Case.

The case admitted by the Court below to be "more nearly akin" (fol. 763) to the present case than any other is *Noyes* vs. *First National Bank* (1st Dept. 1917), 180 App. Div., 162, affirmed *on opinion below*, 224 N. Y., 542.

There it appeared that the Rock Island Railroad Company had opened two special accounts in the defendant bank, which were designated on the books of the bank by the titles "Chicago, Rock Island & Pacific Railroad Company Coupon Account" and "Chicago, Rock Island and Pacific Railroad Company, No. 2 Account." The deposits in both accounts were credited on the books of the railroad company to an account entitled "First National Bank of New York Interest Account." It appeared from the book entries and vouchers made by the railroad company that the purpose of opening the special account and of making deposits therein was to use the money so deposited for the payment, from time to time as it might accrue, of the interest on two of the railroad company's bond issues. *Payment was made directly by the bank from said accounts as the coupons were presented.*

It is important to note that the form of the warrant of the Railroad Company does not appear in the opinion of the Court, but is set forth in the Record on Appeal and is quoted in the *Interborough* case, referred to hereafter, at p. 343 of the opinion as follows:

> "Chicago, Rock Island and Pacific Railroad Company. Warrant in Favor of First National Bank. Address: 2 Wall Street, New York City. August 29, 1905. For deposit in Coupon Account of C. R. I. & P. R. R. Company to meet 6 mos. interest due Sept. 1, 1905, on $17,331,000 of its 5% Bonds of 1913, $433,275.00."

Upon the receivership of the railroad company, the coupon holders claimed to be entitled to the special account as against the Receiver.

Judge Scott, speaking for the Appellate Division, in holding that the relationship created between the railroad company and the bank was simply that of debtor and creditor with respect to the special coupon account, clearly states the contentions of the opposing parties, the defendant's contention being in substance what is contended by the Respondent here.

*If the transfer of funds from a general to a special account, the making of appropriate entries on the corporate books, the issuance of a warrant specifically stating that it was for the payment of coupons, does not create a trust or other equitable interest in the fund thus specifically identified for that purpose in the bank, it is hard to see why in the present case the acts of the parties can lead to any other conclusion. In the Noyes case as in the present case, there were two separate accounts and yet the Court held that the funds in the account containing the specially identified credit were at all times subject to the control of the railroad and therefore, remained the railroad's funds and passed to its receiver.* As stated

in *Taussig* vs. *Carnegie Trust Co.* (1913), 156 App. Div., 519, *infra*, the opening of the two accounts "was a mere matter of convenience."

**The Erb Case.**

The *Noyes* case was recently followed in the Court of Appeals in New York in *Erb* vs. *Banco di Napoli*, 243 N. Y., 45 (1926). In that case, the Kingdom of Italy issued its bonds which provided on their face that principal and interest would be paid at the office of the Banco di Napoli in the City of New York. The coupons contained a like provision. The plaintiff lost three coupons, could not present them for payment, but nevertheless sued the Banco di Napoli for the amount thereof. The Court of Appeals held that there could be no recovery. The decision is peculiarly important because in the language of the Court of Appeals "The Kingdom of Italy had *provided funds* to meet its obligations," and it appeared from the agreed statement of facts "that the Kingdom of Italy has *supplied* the defendant with the *funds* wherewith to pay these coupons * * *." The New York Court of Appeals held nevertheless that the relationship between the Kingdom of Italy and the Bank in New York remained solely that of debtor and creditor, and that the plaintiff could not recover under the third party beneficiary doctrine. In speaking of the *Noyes* case, the Court of Appeals said:

> "The case of *Noyes* vs. *First National Bank of New York* (180 App. Div., 162; affd. 224 N. Y., 542) seems to be directly in point. There it was held that money sent to a bank to pay interest coupons and entered by the bank in a special account for this purpose did not create a trust in favor of the holders of outstanding coupons."

These cases are in principle indistinguishable from the present case and should be followed here. This court in

the recent case of *Empire Trust Co.* vs. *Cahan*, 71 L. Ed. 826, decided May 31, 1927, said:

> "It is very desirable that the decision of the courts of the United States and that of the highest court of the state where the business was done should agree* * *."

The Court below could only distinguish the *Noyes* case by saying that there "the funds were not credited to the bondholders on the books of the agent" (fol. 764). The implication is that in the present case, the fund abroad was credited on the books of the B. C. I. to the Trinidad bank or the draft holder. This is not so. The amount of the draft was credited only to an omnibus Drafts Payable Account "*where it is entered in a folio under the name of the bank whose account has been charged*" (fol. 350)—*in this case the name of K. N. & K.*

**The Interborough Consolidated Case.**

The decision of the Court below in the leading case of *In re Interborough Consolidated Corporation*, (C. C. A. 2nd, 1923) 288 Fed. 334 *certiorari* denied, 262 U. S. 752, is inconsistent with its present holding.

*Facts.* There the question was whether on the bankruptcy of the Interborough Consolidated Corporation a Coupon Account in a New York bank, set up for the payment of coupons under the Corporation's mortgage, was a trust fund, or had become subject to an equitable charge or lien, or had been equitably assigned, so that the holders of unpresented coupons which had matured could claim the fund to the exclusion of the general creditors of the bankrupt. The Court held that there had been no equitable assignment and that the balance in the Coupon Account must be considered a part of the bankrupt's general assets.

It appeared that at the time of the bankruptcy, the Corporation had on deposit with the Empire Trust Company a fund of some $431,000.00, said fund being in the account entitled "Interborough Consolidated Corporation — Interest on Interborough-Metropolitan 4½% Bonds," which had come into existence under the following circumstances: It had been the custom of the treasurer, shortly before any installment of interest on the bonds became due, *to withdraw from the general funds* of the Interborough *sufficient* funds to pay the installment of interest becoming due and to deposit them with the Trust Company, which entered on its books money so deposited in a special account entitled as aforesaid "Interborough Consolidated Corporation—Interest on Interborough—Metropolitan Company 4½% Bonds." *The balance in the account thus created was used solely for the payment of interest.*

Upon presentation of coupons at the office of the Consolidated checks were *drawn by the Interborough* upon the Empire Trust for the several amounts of the coupons presented. *The checks stated on their face that they were to be paid out of the fund for the payment of interest, entitled as aforesaid.* Similar checks were sent to holders of registered bonds. It appears further, from the District Court's opinion, 277 Fed. 249 (where a much fuller statement of the facts is set forth) that at a meeting of the directors of the predecessor company, the Interborough-Metropolitan, the president had stated that in order to facilitate the distribution of dividend, interest and bond payment, *it was desirable to create special deposit accounts by withdrawing from the general funds from time to time, funds sufficient to meet the requirements, each withdrawal to be accompanied by a check in accordance with the by-laws and "to comprise a separate and distinct deposit to cover the exact amount of a full interest payment."* On June 3, 1915, at a meeting of the

Board of Directors of the successor company, the Consolidated, a similar statement was made by the president of the Company.

*Holding.* On these facts the Circuit Court of Appeals held *that no trust, equitable lien or equitable assignment had been created and that the holders of outstanding coupons were but general creditors.*

In the present case, no contract of any kind was made by K. N. & K. with the draft holder, whom nevertheless the Court below found to be the equitable assignee. Nor is there any evidence that K. N. & K. ever lost control of the fund. The holding of the Court below in the present case is inconsistent with its holding in the *Interborough* case.

The lower Court's attempted distinction of its earlier decision in the *Interborough* case is along the same lines as its attempted distinction of the *Noyes* case.

> "There, the mortgagor did not establish a credit on which the bondholders might draw, but drew checks itself to pay the coupons" (fol. 763).

As was said with respect to the Court's comment on the *Noyes* case, K. N. & K. in the present case "did not establish a credit" on which anyone but themselves could have drawn.

**Summary of Noyes and Interborough Cases.**

It is to be noted that in the *Noyes* case, despite the fact (1) that the railroad company had set up a special coupon account, and (2) had transferred to that account certain funds, a portion of its balance, and (3) that the bank was authorized to pay out such moneys without further act of the depositor, and (4) upon the mere presentation of the coupons, nevertheless, this was deemed to be a mere method of procedure. The segregation of

the balance was held *not* to constitute an assignment, but to leave the money wholly within the control of the depositor with the result that it passed to its receiver. And in the *Interborough Consolidated* case it is to be noted that the coupon account was set up by special resolution and that it was stated by the president of the corporation that the purpose was to withdraw the moneys in the coupon account from the general account. *Yet in these two leading cases, it was held that there had been no equitable assignment and that the money was still subject to the control of the depositor and that the fundamental relationship between the bank and the depositor was not affected by the mere book entries.*

### G. Authorities Relied on by Respondent and Court Below Distinguished.

In *Fourth National Bank* vs. *Yardley*, 165 U. S., 634, there was an *existing* bank account in New York and when the owner of that account gave his check on the New York bank, he represented that there was a balance in New York and that *it, that very fund*, would be applicable to and available for the payment of the particular check. There was a present intention to assign, and in equity, a present assignment of that *specific bank account*. It was the *res* in New York that was in reality the subject of the contract, for as the court said:

> "If it was the *understanding* and *agreement* of the parties that an advance about to be made should be a charge on and be satisfied *out of a specified fund*, a court of equity will lend its aid."

The court found that that was the agreement and that the balance in the New York account was the *security* upon which the money was advanced. Certainly in the case at bar Trinidad did not seek security for performance of K. N. & K.'s promise.

In *Coates* vs. *First National Bank of Emporia*, 91 N. Y., 20, the Court held that there was an existing fund in the hands of the New York bankers, *which very fund* it had been presently agreed should be transferred from the Mastin Bank to the Emporia Bank in consideration of the payment by Emporia to Mastin of $5,000.00 The whole basis of that decision, as in the *Yardley* case, was that from all the circumstances of the case, it was concluded that the intention of the parties had been presently to assign *a specific existing fund* in another bank and that the delivery of the checks was simply the means of enabling the assignee to collect the assigned funds. That this is so, appears from the court's statement as follows:

> "In the case before us * * * there was an existing fund in the agent's hands and a distinct contract by the debtor with its creditor *to discharge the liability out of that fund* and to give directions for that purpose."

Such directions were given and of course the transaction thus became wholly executed and the Emporia Bank became a creditor of the New York bankers on their books and the Mastin Bank was discharged.

The same principle underlies *Muller* vs. *Kling*, 149 App. Div., 176, affirmed 209 N. Y., 239, namely the intention equitably to assign *a specific obligation*—the intention to contract respecting a *specific res*. Judge Miller, in his able opinion in the Appellate Division, points out that Muller, Schall parted with their money *on the faith and security of an existing debt or fund*, to wit, the obligation of Invinizio to Scholtz, which was to be collected by Damechy and applied upon the draft. The same view was expressed by the Court of Appeals, citing as authority the *Yardley* case. It hardly can be urged that this unusual case—in-

volving existing collateral security upon the faith of which the very purchase of the draft hinged—can have the slightest relevancy to the ordinary banking transaction involved in the present case, where no particular fund—no *res*—was involved, but merely an obligation on the part of K. N. & K. to provide "sufficient" funds at the time of presentment in the future as a method of "protecting" the draft.

In *Hackett* vs. *Campbell*, 10 App. Div., 523, there was admittedly an assignment of an existing indebtedness as between the assignor and the assignee, the only problem being as to whether or not the third person debtor had waived the contractual rights, which it had, to refuse to recognize such an assignment. The Court held that it had waived these rights and that it was bound to pay attention to the notice which it received of the admitted assignment from the assignor to the assignee.

*Dean (now Mr. Justice) Stone's Discussion.* In its brief below, respondent quoted from an article heretofore written by Mr. Justice Stone in 21 Columbia Law Review 507. The learned Justice, in speaking of the banker in the case of *Legniti* vs. *Mechanics and Metals Nat'l. Bk.* (1921) 230 N. Y., 415, said:

> "Had he actually acquired the credit and specifically appropriated it or a part of it to his undertaking for account of the plaintiff, a very different situation would have arisen and one on which the plaintiff might properly have based a claim that the credit so far as it was an unenforceable one was held by the banker in a fiduciary capacity for the plaintiff."

The *Legniti* case, however, had to do with the ordinary cable transfer transaction where the buyer contracted to buy and the seller to sell a foreign credit *which was clearly to be created in the name of the buyer and which the seller first had to "acquire."*

But the premise on which the writer's conclusion rests is that a credit be "specifically appropriated" to the banker's undertaking, for account of the customer. The discussion is not, therefore, conclusive here because the basic question is left unanswered—What facts show an obligation or intention specifically to appropriate a balance to the banker's obligation and what particular acts of the American banker in effect constitute an irrevocable appropriation without the retention of the right of control? These questions, of course, Mr. Justice Stone was not called on to consider within the scope of his discussion.

Neither did he consider the effect of Section 70 of the Bankruptcy Act referred to in Point III hereof. So that, in reality, his discussion does not advance the determination of the particular questions now before this Court, namely, *was* there here such an agreement and an intention to appropriate a particular fund, and was such appropriation here so irrevocably effected that the foreign balance did not pass to the trustee in bankruptcy.

## CONCLUSION TO POINT I.

*It is submitted therefore that the Court below erred in finding that the bankrupts had equitably assigned their credit in the "Drafts Payable" account before the drafts were presented for payment and actually paid by the B. C. I.*

## POINT II.

**The contract of the parties and the method of its execution did not establish ab initio a fiduciary or agency relationship between the Trinidad Bank and K. N. & K.**

### Preliminary Statement.

The Court below found in favor of the respondent on its second cause of action based on the theory of equitable assignment and found it unnecessary (fol. 769) to consider the first cause of action, i. e. that the bankrupts originally received money from Trinidad in trust.

If this Court reverses the decision of the Court below, it must pass on this first cause of action before dismissing the respondent's petition. It is hoped that the Court will express an opinion on this first cause of action in any event as it is the desire of all parties that the present case as a test case, dispose of as many other claims as possible.

If a fiduciary or agency relationship existed between the Trinidad Bank and K. N. & K., it must have grown from the undertakings of the parties, as found in the book called "List of Foreign Correspondents" (Claimant's Exhibit 1, fols. 418, *et seq.*) and in the book of "Forms and Advices" (Claimant's Exhibit 2, fols. 473, *et seq.*). Before analyzing those exhibits, and in order to determine whether K. N. & K. were mere agents or were independent contractors, the following principles established by the cases and authorities hereinafter referred to (*infra*, page 64 *et seq.*), must be borne in mind.

**A. Fundamental Legal Principles Underlying the Agency Relationship.**

(1) The mere fact that the word "agent" is used does not establish that relationship, if the legal obligations of K. N. & K. were in fact those of independent contractors.

(2) The tests usually applied to determine whether A. is the agent of B. are:

(*a*) Does B. control and direct A.'s activities or is A. merely employed to accomplish, with his own means and by his own methods, the ultimate result desired by B. and for which B. pays a consideration.

(*b*) Do A.'s services bring B. into contractual relations with third parties.

(*c*) Does the alleged principal or agent bear the risk of profit or loss from the transaction.

With these principles in mind, the following analysis of the contractual rights and obligations of the parties will show that the relationship here established between the parties was that of independent contractors.

**B. The Evidence of an Independent Contractor Rather Than an Agency Relationship.**

1. The introductory statement in the List of Foreign Correspondents, which explains the underlying purpose of the service, states that the maintenance of a foreign department by the inland banks involving the carrying of balances abroad "is undesirable" (fol. 419) and that K. N. & K. have aimed for many years to supply the wants of inland banks by extending to them "the privilege of using our *world-wide facilities* for carrying on a foreign exchange business" (fol. 419). It further states

that under the service offered, the inland banks "issue *their own drafts as principals* on the places mentioned in our List of Correspondents," and included in the book (Claimant's Exhibit 1) are 69 pages upon which are enumerated the list of foreign banks which might be drawn upon (fol. 472). The introduction also states (fol. 420) that upon receipt from the inland banks of proper advices and New York funds, K. N. & K.'s advices are sent abroad and "sufficient" funds for the payment of the draft provided to the drawee bank "by transfers of credit from our balance or otherwise."

2. "The Terms and Conditions" which follow the introductory statement (fols. 422, *et seq.*) provide:

> "Upon receipt of advice of draft, accompanied by adequate funds payable at par in New York, we shall promptly forward our advice of the same and provide the drawee with funds *sufficient* for the *payment* of the draft abroad, *by* a transfer of credit from our balance or otherwise, provided the draft is drawn on a bank named in our latest list of correspondents.
>
> "Under this arrangement, *our correspondents, in this country act as principals, and issue drafts in their own names, our name not appearing thereon.* In other words, we are employed merely as the agents of the drawers for the purpose of advising the issue of their drafts and providing the drawee bank with *sufficient funds* to cover their payment."

3. *The advice sent by Trinidad* of the drawing of the draft (Claimant's Exhibit 4, fol. 482), is one of the forms provided by K. N. & K. in the book of forms and advices (Claimant's Exhibit 2) and *must be read in conjunction with the "Terms and Conditions"* as it forms a part of the Drawing Service. In that form of advice appears the following instruction:

"8469B 69B

"Pursuant to the terms and conditions governing your drawing service we have sold draft, bearing the above number, dated, Trinidad, Colo., May 19, 1923.

"For Lit. 24,360.00 and shall thank you to *protect same upon presentation.*

"We remit herewith the sum of $1,191.20 @ rate

4.89 quoted { on Rate Card No. / in Telegram of / Telephone from } 18."

What the obligation of K. N. & K. was, under this instruction from Trinidad, depends upon the meaning of the direction "*shall thank you to protect same upon presentation.*" An obligation to "protect" a draft upon presentation is a personal general obligation to see that the draft is paid.

See

*Wabash St. L. & Pac. Ry. Co.* vs. *Ham* (1885), 114 U. S., 587, quoted *supra*, page 24 and other authorities there relied on.

It appears, therefore, that K. N. & K. was simply paid in advance for their own general obligation to see to it that the draft drawn by the Trinidad bank was paid *at presentation*, despite the fact that Trinidad had no account with the bank upon which it drew the draft.

4. The provision of Claimant's Exhibit 1 that K. N. & K. would provide the drawee "with funds *sufficient* for the payment of the draft abroad," is wholly inconsistent with respondent's theory that there was an obligation assumed by K. N. & K. to "forward" or to "remit" *the* fund or moneys which they received from Trinidad. *They could provide any funds to the foreign*

*bank at any time and by any means, as long as they were sufficient to cause the draft to be "protected" upon presentation.* The significance of the word "sufficient" as refuting the existence of a fiduciary relationship is shown in the *Beecher case*, p. 71 *infra*. Of course, as a practical banking matter, this result would be accomplished by K. N. & K. seeing to it that *at the time when the draft was presented*, K. N. & K.'s credit balance was sufficient to enable the foreign bank, in pursuance of the advice, to pay the draft, debiting the same to the K. N. & K. account. That would be the usual method and *means* of providing "sufficient funds."

5. It was not intended that, and the Drawing Service did not provide that Trinidad in any wise was to control or direct the means or method by which K. N. & K. was to perform their obligation. The complete freedom of method is evidenced by the provision that the sufficient funds could be provided by transfer of credit "or otherwise." This complete absence of control as to the method of effecting the result is a strong indication of the absence of an agency relationship. (See authorities, page 69, *infra*). It signifies rather the obligation of an independent contractor to carry out his contract by whatever means or method he sees fit, provided only he accomplishes the result contracted for and for which the consideration has been paid.

6. Paragraph (13) of the "Terms and Conditions" (fol. 434) states that there are furnished to the inland correspondents by card or telegraph quotation "the rates at which we are prepared to *sell or* provide for the payment of drafts." Thus there is considered under one head and in *pari materia* the rates and obligations with respect to the selling of K. N. & K.'s own drafts and the protection of or provision for the payment of

the inland bank drafts. Of course, there can be no doubt that as to the drafts issued by K. N. & K. as drawer, their only obligation was a general contractual one and not fiduciary. *In re Bolognesi* (C. C. A. 2nd, 1918) 254 Fed., 770. In the minds of the parties, the two transactions were deemed to be essentially similar. That the protection of the inland bank's draft was intended to produce no different liability than the sale of K. N. & K.'s own draft, is further evidenced by the provision of paragraph (14) of the "Terms and Conditions" (fol. 436). There it is provided that where an inland bank desired to sell a draft "on places not on our (K. N. & K.) list," such draft "should be bought" directly from K. N. & K., i. e., Trinidad should furnish the inland customer with a draft drawn by K. N. & K., and in such a transaction, *the same procedure as to payment by the inland bank to K. N. & K. and advice abroad was pursued as where Trinidad was the drawer of the draft.*

7. The provision at the end of Paragraph (13) of the Terms and Conditions (fol. 435) provides that if the inland bank sends insufficient funds, K. N. & K. has the option of refusing to send their advice abroad, or "we may advise the draft abroad and require payment to us by the remitter of the deficit at the correct rate." This indicates that even if K. N. & K. did not receive American Dollars equivalent to the foreign amount of the draft at the rate stated in the rate card, *it nevertheless could perform its obligation.* If it did so under such circumstances, it is clear that in performing that obligation, it could not be transmitting a fund, but must be employing its own credit.

8. The steps taken by K. N. & K. to perform their obligations in accordance with the instructions received

from Trinidad in Claimant's Exhibit 4, negative the contention now advanced by Trinidad that the obligation was to transmit a fund. In order to "protect the draft upon its presentation," K. N. & K. sent advices to the main office and branch office of the B. C. I. In the first form of advice, the B. C. I. was directed "*to protect* to the debit of *our* account the drafts as per particulars on the annexed copies," and in the second was sent the instruction "Please *honor* the above listed drafts, charging same to *our* account." The list included not only drafts drawn and advised by the inland banks under the drawing service, but also drafts drawn directly by K. N. & K. Here are no instructions to establish a credit for Trinidad or anyone else, or to transfer any moneys to Trinidad or anyone else, but solely the instruction to honor the draft, charging the same, to wit, the draft, to the K. N. & K. account. Here we have the usual every day banking transaction where the American banker advises his foreign correspondent that he has drawn a draft and requests him to honor it and charge it to the banker's account. *The situation only differs from the ordinary one, in that K. N. & K. in addition to protecting its own drafts, assumed an obligation to protect in a similar way the drafts of other drawer banks.*

### C. The Use of the Words "Principal" and "Agent" Are Not Controlling and Do Not Negative the Conclusion that the Parties Dealt as Independent Contractors.

To meet the cumulative effect of all the foregoing provisions showing the existence of an independent contractor relationship, the respondent relied below upon the use of the words "principal" and "agent" (Claimant's Exhibit 1 and 2, fols. 420 and 477). But the courts

have held in numerous cases that describing the relationship of parties as "partners" or as "agents," does not make them such, if their respective obligations, as a matter of law, do not establish such relationship.

*Beecher* vs. *Cosmopolitan Trust Co.* (1921), 239 Mass., 48; discussed at length, p. 71, *infra;*

*St. Regis Paper Co.* vs. *Hubbs &c. Paper Co.* (1923), 225 N. Y., 30;

*Sloan Shipyards Corporation* vs. *U. S. S. B. E. Fleet Corporation,* (1922), 258 U. S., 549;

*Casement* vs. *Brown* (1893), 148 U. S., 615;

*Employers' L. A. Corporation* vs. *U. S. S. B. etc. Corporation* (C. C. A. 2nd, 1923), 290 Fed., 182;

*Bendix* vs. *Staver Carriage Co.* (1912), 174 Ill. App., 589, 595;

*Petition of Williams* (C. C. A. 1st, 1924), 297 Fed., 696;

2 *Corpus Juris*, 423.

Mr. Justice Stone in 21 Columbia Law Review, page 521, said:

> "Nor is the nature of the banker's liability determined by referring to him as the 'agent of the depositor.' An agent may assume either a contractual or fiduciary liability with respect to money paid to him by the principal. The question is which kind of a duty did he assume, a question which can be answered only by inquiring as to the intention of the parties as evidenced by their acts interpreted in the light of the customary method of transacting business."

In *St. Regis Paper Co.* vs. *Hubbs & Hastings Paper Co.* (1923), 235 N. Y., 30, the court said at p. 36:

> "Even if for proper interpretation the contracts are to be read in the light of the collateral correspondence, it appears that the word 'agent' was used by the parties, not meaning 'one who acts for a principal,' *but in the not unusual sense of 'one with or through whom another transacts business'* and that the word 'commissions' was used for the equivalent of 'profits.' * * * The disposition of the case is, therefore, placed on broad fundamental grounds and not an narrow technicalities which might serve only to conceal the real obligations of the parties."

That the courts themselves have used the word "agent" in a loose sense appears from the leading case of *Moore* vs. *Potter* (1898), 155 N. Y., 481, where it was urged that an unpaid vendor who sold the merchandise for account of the buyer occupied a fiduciary relationship to the buyer, because the earlier cases in New York had said that one of the remedies of an unpaid seller was to sell the merchandise "as agents of the vendee." The court, in referring to the earlier use of the word "agent" said at p. 487:

> "*Clearly, the use of the words 'as agent of the vendee' was not intended as a determination that the relation between the parties was that which ordinarily exists between a principal who owns property and an agent* who may be authorized to manage or sell it. But *it is a general expression which has been somewhat inaccurately used to define the right of a vendor to make a resale and hold the vendee responsible for his loss.* It is quite manifest that a resale made under such circumstances is not made by the vendor strictly as the agent of the vendee, but he acts for himself in disposing of the property for the purpose of ascertaining the actual damages he may sustain."

In the *Fleet Corporation* cases, *Sloan Shipyards* vs. *U. S. S. B. E. Fleet Corporation* (1922), 258 U. S., 549,

a contract contained the provision that the Fleet Corporation was "representing the United States of America." It was urged, therefore, that the United States was the contracting party and that (a) it could not be sued in the District Court and that (b) it had a priority in bankruptcy. This Court held, however, that an examination of the contract as a whole showed that the Fleet Corporation contracted as a principal and independent contractor.

REASONS FOR THE USE OF THE TERMS "PRINCIPAL" AND "AGENT" IN THE PRESENT CONTRACT.

The reason for the use of the words "principal" and "agent" is clear if the provisions of the Service and the scheme employed are considered as a whole. It is fundamental to bear in mind that Trinidad, the inland bank, desired to appear to *its* customer as having the facilities of issuing *its own drafts* upon foreign banks, without being required simply to procure for the customer a draft from a New York banker. For this reason, the inland banks desired to "issue *their own* drafts *as principals*." That is, not to sell drafts of the New York bankers merely as the agent of those bankers. To accomplish the result sought, the scheme was that *K. N. & K. dealt only with the inland bank* and was to have no contractual relations either with the customer of the Trinidad bank in Colorado or with the payee of the draft which Trinidad drew. The only one to whom K. N. & K. was to have any obligation under the plan was the inland bank. Having, therefore, in the Drawing Service described Trinidad as the "principal" in the transaction in order to emphasize the fact that K. N. & K. had no relation with the customer in Colorado or the payee, and that the sole function of K. N. & K. was to have Trinidad's draft paid, it is stated: "in other words,"

K. N. & K. was the "agent" of Trinidad. Having em
ployed the word "principal" to define the relation o
the Trinidad bank to its customer, the correlative wor
"agent" was likewise employed. As in the *St. Regi*
*Paper Co.* case "agent" meant "one with or throug
whom another transacts business" and as in the *Flee*
*Corporation* cases "representing the United States o
America" did not mean an agency, so here the mer
use of the term "agent" does not of itself determine tha
K. N. & K. received the dollars from Trinidad in a fidu
ciary capacity.

### No Technical Agency.

That there was no technical agency or fiduciary rela
tionship follows from the nature of the obligation whic
K. N. & K. assumed. The application of such obligatio
to the tests which have been applied to determine whethe
a fiduciary relationship or that of an independent con
tractor has been established indicates clearly that n
fiduciary obligation was assumed by K. N. & K. Thes
tests have been stated above to be:

(*a*) Control of the means of performance;

(*b*) Bringing the principal into contractual relation
with the third party;

(*c*) The assumption of risk of profit and loss.

It already has been shown that Trinidad did not con
trol or direct the means by which K. N. & K. was to ac
complish the ultimate result for which the considerati
was paid by Trinidad in advance. K. N. & K. ha
"*world-wide facilities*" (fol. 419) for carrying on an ex
change business, and it was for the use of *its* facilitie
that the inland bank had contracted.

Mechem on "Agency" has stated the difference be

tween an agent and independent contractor in language which is peculiarly applicable to the present case. In Volume I, Mechem, Sec. 25, it is sated:

> "*Agency defined.*—The word agency, when used in its broad meaning as pointed out in the preceding chapter, *indicates the relation which exists when one person is employed to act for another.* In this aspect, it has, in our modern law, three chief forms: 1. The relation of principal and agent; 2. The relation of master and servant, or, in the more modern phrase, the relation of the employer and employee; and 3. *The relation of employer or proprietor and independent contractor.* All of these have some points of similarity but, at the same time, many aspects of real distinction."

And in Section 40, it is stated:

> "*How agent compares with independent contractor.*—Although all three are, in a large sense, agents, yet in ordinary legal usage the agent—and the servant also—is further to be distinguished from the 'independent contractor,' who is one who exercises some independent employment, in the course of which he undertakes supplying his own materials, service and equipment, *to accomplish a certain result*, not being subject, while doing so to the direction and control of his employer, but being responsible to him *for the end to be achieved* rather than for the means by which he accomplished it."

In other words, where the supposed "agent" is simply employed *to effect a result* and the supposed principal has no control over the method or means of performance, the relationship is that of independent contractors, although it may be stated that one person is employed to do something for the other as his "agent."

The *second test* has not been met, for it already has been shown that K. N. & K. was not employed to bring

the Trinidad bank into any contractual relations with third parties. In Dean Huffcut's valuable analysis of the principles of agency, at page 12 it is said:

> "An agent, therefore, is a representative who creates bifactoral obligations to which his principal is a party. These are usually contracts; but other concepts of the law fall within the classification, namely gratuitous undertakings, estoppel and deceit."

K. N. & K. was not employed to set up a credit in the name of Trinidad with the B. C. I. thus establishing a debtor and creditor relationship between the two. That is the very thing which the Drawing Service was intended to avoid. (See preliminary explanation, fol. 419). The B. C. I. assumed no obligation to Trinidad. It had no account on its books in favor of Trinidad. Its contractual relations remained solely with K. N. & K. to whose account it was directed to debit the draft upon its presentation. Even if there were an equitable assignment as the lower court has held, the assignee would be the holder of the draft and not the Trinidad bank.

The *third test* in determining the existence of an agency relationship is whether the alleged "principal" bears the risk of profit or loss in the transaction. If the "agent" bears the risk of profit or loss, he is an *entrepreneur* and is an independent contractor and not an agent. For discussion of this test, see 20 *Columbia Law Review*, 333; 22 *Columbia Law Review*, 576.

In the present case K. N. & K. undertook for a certain number of American dollars paid in advance to have a draft for a fixed amount of lire paid on presentation. K. N. & K. thereby assumed the risk of profit or loss, which might result from the decrease or increase in the value of the lire prior to the presentation of the draft. In doing so, they became *entrepreneurs* and in their rela-

tions to the Trinidad bank must have acted as principals and independent contractors.

In support of this conclusion is the stipulated fact at folio 70, that the rate on the day of the transaction was .0489 per lire and that "in fixing the aforesaid rate the bankrupts fixed an amount which was *estimated* by them to be sufficient to leave them a profit in the transaction."

**D. Leading Recent Cases Holding that the Relationship Established Was Not a Fiduciary One.**

The facts in *Beecher* vs. *Cosmopolitan Trust Co.* (1921), 239 Mass., 48 are in all material respects "on all fours" with those in the present case. On September 21, 1920, Beecher, the plaintiff, paid to the defendant trust company $500.00 and 30¢ postage for a "remittance order" for 24,270 Roumanian Lei payable to Mordchi Berman in Roumania. He received a numbered receipt called "remittance order," which contained the terms upon which the Trust Company agreed to remit. The material terms, and their similarity to the facts in the present case should be noted, were:

> "1. It is expressly agreed that The Cosmopolitan Trust Company *acts as agent only* for the sender.
>
> "2. The Cosmopolitan Trust Company, its correspondent or agent, is to forward the money from any European post-office to the required address. * * *
>
> "4. Refunds will be made at rate of exchange prevailing on date of refund."

On the day that the remittance order was issued the defendant Trust Company had a net credit balance with the foreign bank in Bucharest in the amount of 303,424.25 Roumanian Lei and an entry was made on the books of the Trust Company crediting the foreign bank

with 24,270 Roumanian Lei. (The entry thus made is of the same kind as that made by K. N. & K. in their so-called Memorandum Account, Trustee's Exhibit I, fol. 565). It appeared that it was the practice of the Trust Company to send advices of a remittance by every convenient sailing, and in accordance with this custom, on September 24th the Trust Company sent to the foreign bank by mail a letter of advice which read:

> "Please execute the following money orders *to debit of our account*,"

followed by a list of numbers of remittance orders, including the one issued to Beecher. (This is in substance the same as the advices, Claimant's Exhibit 6, fols. 487 *et seq.*, which state "Please protect to the debit of our account, the drafts as per particulars upon the attached copies," and Exhibits 6A to 6E which provide: "Please honor the above listed drafts charging the same to our account").

Upon receipt of Beecher's money, it was immediately placed with the general funds of the Trust Company. On the day after the advice was sent abroad, the Commissioner of Banks took possession of the Trust Company and by cable stopped payment by all foreign correspondents. The plaintiff demanded of the Trust Company and the Commissioner of Banks a refund of the $500.00 paid.

In holding that Beecher, the plaintiff, was but a general creditor of the Trust Company and that *no trust relationship was created*, the Supreme Court of Massachusetts in a unanimous opinion said:

> "Upon the foregoing facts the plaintiff contends that a trust attached to the $500.00 when that amount was delivered to the defendant trust company; that the company and the bank commissioner thereafter held that money as trustee,

and not as debtors, until the object for which the money was left with the defendant trust company was accomplished or it was returned to the plaintiff. As no contention is made that the trust arose through the fraud or bad faith of the company or its officers in receiving the money of the plaintiff with knowledge of its insolvency, the argument that there was a trust created by the delivery of the money to the defendant trust company for remittance must stand or fall upon the fact, or the absence of fact, that the money was received by the defendant trust company as a special deposit for transmission to its correspondent bank in Roumania. *Freeman's Bank* vs. *National Tube Works Co.*, 151 Mass., 413, 418, 24 N. E., 779, 8 L. R. A., 42, 21 Am. St. Rep., 461; *Farber* vs. *Dane*, 204 Mass., 412, 416, 418, 90 N. E., 859, 27 L. R. A. (N. S.), 808. Upon consideration of the receipts and remittance order, in the light of all the admitted facts, *we are of opinion that the obligation of the defendant trust company to the plaintiff created by the delivery of the money was not to hold that money separate and apart from its general funds until the remittance order should be presented and honored, but was a contract obligation based upon the payment of the money to have funds in Bucharest with a bank, which funds should be* **sufficient** *to insure the payment of the order on presentation. In a word, what the plaintiff accomplished by the payment of the money was the receipt of an agreement by the defendant trust company that it would procure and* **provide funds** *in Roumania to meet the order which it had sold and delivered to the plaintiff when that order should be presented for payment. It was not contemplated by the plaintiff that the money itself should be remitted or that the trust company should not use the money paid to it as its own pending the performance of the agreement with the plaintiff.* Its failure to perform gave rise to an action in contract, and not to a suit cognizable in a court of equity. *Taussig* vs. *Carnegie Trust Co.*, 213 N. Y., 627, 107 N. E., 1086; *Legnti* vs.

*Mechanics & Metals Nat. Bank of New York*, 230 N. Y., 415, 130 N. E., 597."

It is to be noted particularly that in the portion of the opinion italicized the Court emphasizes a distinction between the obligation to transmit a specific fund and an obligation "to *have* funds in Bucharest with the bank which fund should be *sufficient* to insure the payment of the order on presentation." The Court uses the word "sufficient" funds in the very sense in which it was used by the contracting parties in the "Terms and Conditions," namely, as representing a general contractual obligation to provide funds generally to meet the *order* in the *Beecher* case and to meet the *draft* in the present case upon their presentation.

It would seem that the claim of the existence of a trust relationship is completely disposed of by reference to the *Beecher* case alone, where the bank is specifically referred to as the "agent" of the sender and as K. N. & K. was in this case. Particularly is this so in the light of the fact that the *Beecher* case was cited with approval by the New York Court of Appeals in *Equitable Trust Co.* vs. *Keene* (1922), 232 N. Y., 290 at 295 and that its conclusions, in part, are predicated upon two recent New York authorities, the *Taussig* and *Legniti* cases, to which reference now will be made.*

In *Legniti* vs. *Mechanics & Metals National Bank* (1921), 230 N. Y., 415, the plaintiff wanted to transfer some money to Naples at once. He made his arrangements for this purpose with A. Bolognesi & Company, New York bankers, by purchasing a cable transfer from them. He received a bill which read "cable transfer to Italy to pay by cable to Banca Commerciale Italiana,

*See quotation from this Court's recent opinion in *Empire Trust Co.* vs. *Cohen*, quoted supra at p. 51, to the effect that "It is very desirable that the decision of the courts of the United States and that of the highest Court of the State where the business was done, should agree * * * ."

Napoli, advice to be forwarded by cable from New York (followed amount and value of exchange and terms of payment)." Plaintiff made payment to Bolognesi by check which was subsequently collected by the latter through deposit in its account with the Mechanics and Metals National Bank. The cable was never transmitted by Bolognesi and on the following day the latter made a general assignment for the benefit of creditors, which resulted later in the filing of a petition in bankruptcy. Bolognesi was indebted to defendant, the Mechanics & Metals National Bank, in offset of which indebtedness the latter wished to hold all balances remaining on deposit with it to the credit of Bolognesi. Said the Court at p. 423:

> "This action has been brought by Angelo Legniti upon the theory that A. Bolognesi & Co. became his agents for the sending of 18,000 lire to Naples, Italy, and that as the money was not sent, he may recover it from the bank into whose possession it can be traced. *The bank, he claims, holds it, charged with a trust to pay it to him; it is his money, he says, as he never lost title to it. We do not think there is evidence here of any trust.* * * * It will be noted that the bill presented to the plaintiff late in the afternoon of February 10th, above quoted, upon which the plaintiff parted with his money, stated that he, Mr. Angelo Legniti, bought of A. Bolognesi & Co. cable transfer to Italy—to pay by cable to Banca Commerciale Italiana. *This was not the case of a specific sum of American money being sent to Naples after being exchanged for lire. It was a case of* 18,000 *lire being needed in Naples and the purchase of A. Bolognesi & Company's credit* with the Banca Commerciale Italiana for this amount which credit was to be used by and for the benefit of Legniti. * * We are naturally impressed, as anyone must be, with the fact that the plaintiff gave his money to establish a relative value or worth in Naples and that the receiver kept the money and did not

deliver the value and that this money the bank now holds. Why should not the plaintiff get it back? *Upon the failure of A. Bolognesi & Co. many claims sprang into existence besides this of the plaintiff and it is the duty of the courts as far as possible to adjust these relationships according to well established principles, usages and customs.* • • •

"There were also many other claimants to the assets. TO ESTABLISH A RULE THAT IN A CASE LIKE THIS THE PLAINTIFF BECOMES A PREFERRED CREDITOR; THAT THE TRANSACTION IS IN THE NATURE OF A TRUST, AND THAT CHECKS DEPOSITED WITH BANKS UPON THE PURCHASE OF CREDIT ARE TRUST FUNDS HELD FOR CERTAIN AND SPECIFIED PURPOSES, IS APT TO LEAD TO MUCH CONFUSION, ESPECIALLY WHEN THOSE WHO HAVE DEVELOPED THIS METHOD OF DOING BUSINESS INTO A WELL ESTABLISHED CUSTOM HAVE NEVER TREATED THEM AS SUCH."

Also, at p. 420:

"There is a marked distinction between these transactions which I have just described and a direction to a bank or other person to transmit a certain specific sum of money to a person abroad. In such cases the bank or transmitter is the agent of the person paying the money, and until the money is sent holds it as agent or trustee for the owner. Such were the cases of *Musco* vs. *United Surety Company*, 132 App. Div. 300, and *People ex rel Zotti* vs. *Flynn*, 135 App. Div. 276. In these latter transactions, the intention of the payer is that the money he gives to his agent shall be sent abroad. It is the amount which he gives that is to be transmitted. How it is sent may be immaterial to him. If there be time, currency might be purchased and sent. If not, it may be transmitted in any form recognized in financial circles. It is not at all necessary that the sender or agent have credit in the place to which the money is to be sent. On the other hand, in the contract for credit it is not a specific sum which is to be sent but rather a specific credit which is to be pur-

chased. The amount paid varies with the market. The actual thing that is done by the sender in both of these cases may or may not be the same, but the practice of the merchants and banks has recognized a difference; so have the courts."

See also beginning of opinion containing long discussion on purchase of credit.

It is, of course, recognized that there is a factual difference between both the *Beecher* case and the *Legniti* case and the case at bar, in that in the former cases the customer dealt directly with the banker making the arrangements for payment abroad, while in the present case the respondent is not the purchaser of a draft, money order or cable transfer, but is an intermediate party contracting with the banker. This factual difference, however, is unsubstantial in that the obligation of the banker in both cases, toward the customer in the first instance and toward the inland bank in the present instance, is the same. In both cases it is an obligation to provide for the payment abroad, in the one case of the banker's own draft and in the other case of the draft issued by the inland bank. In both cases the underlying obligation is to provide "sufficient" funds abroad.

The principles underlying *Beecher* vs. *Cosmopolitan Trust Co.* and *Legniti* vs. *Mechanics Bank*, have been uniformly applied by the Federal and State courts. In fact no case in any jurisdiction has been found which in any wise questions their authority. *The principles underlying them have become a part of international banking transactions.* The leading additional cases are:

*Gravenhorst* vs. *Zimmerman* (1923), 236 N. Y., 22;

*Strohmeyer & Arpe Co.* vs. *Guaranty Trust Co.* (1st Dept., 1916), 172 App. Div., 16;

*Safian* vs. *Irving Natl. Bank* (1st Dept. 1922), 202 App. Div., 459, affd., no opinion 236 N. Y., 513;
*Samuels* vs. *E. F. Drew & Co.* (C. C. A. 2nd., 1924), 296 Fed., 882.

Cases involving letters of credit are also persuasive on this point.

In *Taussig* vs. *Carnegie Trust Company* (1st Dept., 1913), 156 App. Div., 519, affirmed no opinion, 213 N. Y., 627, the defendant Trust Company agreed to issue to plaintiff, who had a general account with the Trust Company, a letter of credit for £600 0 0 payable at the rate of £100 0 0 monthly in exchange for his agreement to have deposited with the defendant his pension of $500.00, also payable monthly. *A new account* was opened on the defendant's books termed "letter of credit account" to which were credited the various deposits of the pension and against which were charged the drawings under the letter of credit. The defendant bank failed at a time when the "letter of credit account" showed a credit balance of $2,920.82 to which the plaintiff claimed to be entitled as a preferred creditor. The court dismissed the complaint, saying at p. 521:

> "*The relation existing between the plaintiff and the trust company, at the time the latter became insolvent, was that of debtor and creditor.* The opening of the account and designating it 'letter of credit' was *a mere matter of convenience* to the trust company. It did not hold the money credited to that account in trust for the plaintiff and his interest was precisely the same in that credit as in the credit to the other account, and in neither case was he entitled to a preference. (Citing cases)."

The Court in the *Taussig* case relied upon *Kuehne* vs.

*Union Trust Company* (1903), 133 Mich., 602. That case is best analyzed in the language of the opinion:

"Hooker, C. J.—One, Milani of Detroit, contemplated a trip to Europe and had a conversation with the savings teller of the City Savings Banks, who advised him to take from said bank a letter of credit and who explained to him the advantages of doing so instead of carrying a large sum of money about his person. Milani subsequently brought to the bank a check upon it drawn by his employer for $500.00 and drew the money from another officer. He put $100.00 in his pocket and paid $400.00 to the aforesaid teller who issued to him a letter of credit for £80 0 0. Nothing further passed between them. * * * He (the teller) entered Milani's name on a signature card and wrote upon it 'guarantee for a letter of credit.' This was done to prevent any portion of said sum being drawn except as against the letter of credit, so that if a personal check of Milani had come to the bank not drawn on that letter of credit it would not have been honored. Milani drew a draft for $241.11 to the order of the plaintiffs, but before the check was presented and cashed by the plaintiffs the City Savings Bank failed. It is the petitioner's claim that the $400.00 paid by Milani for the letter of credit was paid and received by the bank for the specific purpose of meeting the obligation to petitioners under the letter of credit; that it was so treated by the bank; and since the fund in which it was placed was never depleted below the amount of this trust fund that petitioners are entitled to be paid in full. Upon the hearing the Circuit Court in Chancery held otherwise and denied the prayer of the petition. 'We think petitioner's position untenable. *Milani paid his money to the bank for an undertaking to pay him through others, on demand, a lesser amount. This obligation was honored by other bankers under some arrangement between the banks. This fund was never paid or received upon trust conditions and there is nothing to justify giving the priority*

*over other creditors.* The memorandum on the card was fully explained as precautionary merely, and not as giving Milani rights superior to those of any other depositor. The decree is affirmed.' "

The *Taussig* case and the *Keuhne* case involved moneys deposited with the bank to secure or indemnify the bank against the issuance of a letter of credit. They clearly held that money so deposited *though specially identified on the bank's records,* did *not* constitute a trust fund for a particular purpose and that the customer was not entitled to have a specific fund returned in the event of insolvency. *Those decisions go far beyond the necessities of the present case.*

**E. Principles Deducible from the Foregoing Authorities as to Existence of Fiduciary Relationship.**

It is evident that the foregoing recent cases have thoroughly considered in their various phases the principles underlying foreign credits and foreign exchange. The analysis of these cases has shown that the Courts have divided these transactions into three classes:

1. If A purchases from an American banker his draft in foreign currency upon a foreign bank and procures such draft from the American banker, he has procured what he desired in the negotiable obligation of the banker. The transaction is executed and A has become merely the owner of the banker's general obligation on the draft.

*In re Bolognesi* (C. C. A., 2nd, 1918), 254 Fed., 770;

*Legniti* vs. *Mechanics & Metals National Bank* (1921), 230 N. Y., 415.

2. If A goes to the American banker and pays him American dollars and the banker contracts to establish

a credit for a definite amount of foreign currency in a foreign bank in the name either of A or A's nominee, then the contract is not that a specific sum is to be sent abroad, but rather that a specific credit is purchased and what A gets is the banker's contract to establish that credit for that definite amount. This contract is executory as distinguished from Class 1, but like Class 1 results only in A obtaining the general obligation of the banker.

*Legniti* vs. *Mechanics & Metals National Bank* (1921), 230 N. Y., 415;

*Gravenhorst* vs. *Zimmerman* (1923), 236 N. Y., 22;

*Beecher* vs. *Cosmopolitan Trust Co.* (1921), 239 Mass., 48.

*American Express Co.* vs. *Cosmopolitan Trust Co.*, 239 Mass., 249;

*Foreign Trade Banking Corporation* vs. *Cosmopolitan Trust Co.*, 240 Mass., 413;

3. If A goes to a New York banker and directs the banker to transmit a certain specific sum of money to a person abroad the banker is the agent of the person paying the money and until the money is sent will hold it as agent or trustee for the owner. In this class the intention of the payer is that the money he gives to his agent shall be sent abroad. It is the amount which he gives which is to be transmitted.*

*Legniti* vs. *Mechanics & Metals National Bank* (1921), 230 N. Y., 415;

*It is suggested that in this class of cases also, the promise of the banker is the real consideration for the payment and the customer relies alone upon the general credit of the banker. Therefore, it may well be that even in this class of cases the relationship should be held non-fiduciary as it is in England. See Mr. Justice Stone's comments, quoted at page 84, *infra*.

*Musco* vs. *United Surety Company*, (1st Dept., 1909), 132 App. Div., 300, (N. Y.); *People ex rel Zotti* vs. *Flynn* (1st Dept., 1909), 135 App. Div., 276, (N. Y.).**

The difference between the transactions in Classes 2 and 3 is this: that in class 2 where the establishment of a credit is contracted for the banker undertakes to establish a credit for a definite amount in foreign currency and thus assumes the risk of profit or loss from the transaction, inasmuch as the consideration received by him from his customs has been fixed. In Class 3, on the other hand, the transmission case, in the language of Judge CRANE:

> "it is the amount which he (the customer) gives that is to be transmitted."

The banker assumes no risk of profit or loss, he undertakes to establish no definite credit in foreign currency, but undertakes only to pay to the customer's nominee the foreign equivalent of the amount received in dollars. This distinction is recognized in the opinion of the New York Court of Appeals in the *Leguiti* case where Judge CRANE, p. 420, says:

> "There is a marked distinction between these transactions which I have just described [a cable transfer or contract to establish a foreign credit—Class 2, *supra*] and a direction to a bank or other person to transmit a certain specific sum of money to a person abroad [Class 3, *supra*]. In such cases the bank or transmitter is the agent of the person paying the money, and until the money is sent holds it as agent or trustee for the owner. Such

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**Mr. Justice Stone's comment on this 1st case is: "It is difficult, therefore, to interpret the undertaking of the banker in that case as being anything more than a contractual obligation to procure a foreign credit for the depositor by the usual methods of exchange" (P. 521 of his article).

> were the cases of *Musco* vs. *United Surety Company* (132 App. Div. 300), and *People ex rel Zotti* vs. *Flynn* (135 App. Div. 276). In these latter transactions the intention of the payer is that the money he gives to his agent shall be sent abroad. *It is the amount which he gives that is to be transmitted. On the other hand, in the contract for credit it is not a specific sum which is to be sent but rather a specific credit which is to be purchased.* The amount paid varies with the market. The actual thing that is done by the sender in both of these cases may or may not be the same, but the practice of the merchants and banks has recognized a difference; so have the courts."

The decision in the *Leguiti* case has been regarded as a landmark by those engaged in the international exchange business. The principles it lays down have been accepted by traders in exchange and by the Courts of sister states. No claim has been advanced that those principles in any wise lead to an injustice. On the contrary it must be evident that an attempt to make an international banker or dealer in foreign exchange a fiduciary upon every occasion that he contracts to sell his foreign credit would lead to endless confusion in the banking world. For this reason counsel for New York bankers were granted leave to and did file briefs *amici curiae* in support of the argument of the Mechanics & Metals National Bank in the *Leguiti* case. All of such counsel earnestly urged that the establishment of a rule under which an agreement to sell a foreign credit would be construed as imposing a trust upon the dealers would be a great hindrance to American banking.

Mr. Justice Stone, in the article already quoted on "Some Legal Problems Involved in the Transmission of Funds," 21 Columbia Law Review, 507, showed his concurrence with the conclusion reached in the recent cases relied upon herein by saying (page 522):

"The great volume of litigation which has sprung from this simple banking transaction in the United States as contrasted with the English experience can only be attributable to the disposition of the courts in this country to impose on an important class of business transactions, a rule of law which does not conform to established business practice, and is not adapted to the economic needs of the business community.

"*The recent decisions of the courts of New York and New Jersey in the case of foreign exchange holding that the obligation of the banker is contractual only, evidence a more just appreciation and exact appraisal of the importance of the method of conducting the banking business in determining what the undertaking of the banker is.* **The principle of decision in those cases ought to be extended and applied generally to those cases where bankers undertake to effect payments of money for account of their customers in the ordinary course of the banking business whether the exchange element is present or not.**

"*The extension of the rule in the Legniti case generally to all cases of deposits of funds with a banker for transmission where there is no stipulation that the banker shall keep the deposit segregated as a trust fund, would not in any way limit the application of the rule that, when property other than current funds is received by the banker for account of his customer, it is to be treated legally as a quasi-trust fund.* We have already seen that paper entrusted to a banker for collection is so held by him although he is treated as only a debtor for the proceeds when collected. Bankers do not customarily use such property in their general business as bankers hence there is no custom or practice to rebut the common law presumption that such property is received in a fiduciary capacity."

As already shown the Massachusetts Supreme Court in the *Beecher* case concurred in the foregoing views.

**F. Obligation of K. N. & K. Even Less Susceptible of Interpretation as a Fiduciary Obligation than Bankrupt's Obligation in Legniti and Beecher cases.**

In the *Legniti* and *Beecher* cases, the bankrupt's obligation was to establish a credit for or to make a payment to a third person in foreign currency and it was held that the American dollars paid to the banker were not received in a fiduciary capacity. Those cases are surely much more analogous to the remittance cases classified under Class 3, *supra*, and relied on below by the respondent, than was K. N. & K.'s obligation here. That obligation, as already shown, was not to establish a credit for or make a payment to a third party, but was, in its essence, solely to see to it that K. N. & K. *themselves* had a sufficient credit balance with the B. C. I. at the time of the presentation of the draft, to the debit of which the draft could be paid in pursuance of the directions contained in K. N. & K.'s advice (Claimant's Exhibits 6 and 6D). It was in the consideration of this executory promise that the American dollars were paid in advance by the Trinidad Bank.

**G. The Hotchkiss Case in this Court Has Clearly Recognized the Principles Underlying the Trustee's Contentions.**

This Court has laid down in clear language the distinction between the line of cases relied upon by the respondent in the lower courts, and the rule applicable in the present case, by pointing out that for a deposit of funds to constitute a trust, *it must be intended not merely that the depositor's balance should be increased by that amount in order to enable it to carry out its contract obligations, but it must be intended that the very fund deposited "should be appropriated specifi-*

*cally" for the purpose indicated by the depositor.* In *National City Bank* vs. *Hotchkiss* (1913), 231 U. S., 50, a bank sought to retain as against the trustee in bankruptcy of a stock broker certain securities which the bankrupt had delivered to the bank on the eve of the bankruptcy. The securities had been obtained by the bankrupts through the use of moneys which had been loaned to them by the bank for that purpose, which funds, however, had been placed to the general credit of the bankrupts, and with the knowledge of the bank, was subject to the absolute disposition of the bankrupts. In holding that the bank could not retain the securities which had been procured by the bankrupts by use of the funds thus made available, Judge HOLMES said at p. 56:

> "In dealing with transactions of this kind, we may go far in giving them any form that will carry out the mututally understood intent * * *. *But if the intent was doubtful or inconsistent with the legal effect of dominant facts, it must fail.* * * * So that, even if we take it as a corollary of what was understood, that the use of the clearance loan was expected to enable the firm to repay the loan, it *does not appear to have been expected that the proceeds should be appropriated specifically to that end, but simply that the addition of such proceeds to the general funds of the firm would enable the latter to pay within the time allowed.*"

**Conclusion as to Point II.**

It is submitted, therefore, that this Court must hold that there was no trust with respect to the $1,191.20 which was sent to K. N. & K. with Claimant's Exhibit 4 (fol. 482), but that K. N. & K. received it solely as independent contractors and as payment in advance for the obligation of K. N. & K. to "protect" the Trinidad

draft "upon presentation." The dominant purpose of the Drawing Service was to enable Trinidad to avail itself of the world-wide credit facilities *of K. N. & K.* The latter were obligated, *not* to forward or remit any particular fund, but to employ their facilities already existing to provide the B. C. I. "with sufficient funds" (whatever their source) at presentation to pay the draft to the debit of K. N. & K.'s own account, *just as in case of drafts drawn by K. N. & K. themselves.*

## POINT III.

**Under Section 70a (3) and (5) of the Bankruptcy Act, the debt from B. C. I. to K. N. & K. vested in the Trustee as of the date of the filing of the petition in bankruptcy. The rights of the parties became fixed upon that date and the subsequent acts of the Receiver cannot change those rights. But the subsequent acts of B. C. I. are most persuasive evidence of the soundness of the Trustee's contentions.**

The respondent attempted to obtain comfort from some of the letters and cables interchanged between the receiver and the B. C. I. after the filing of the petition. Those communications simply set forth the bookkeeping mechanics necessary to effect the payment to the receiver. If they have any effect, they and their results are *most pursuasive evidence of the fact* that the B. C. I. recognized K. N. & K. as its creditor and as the owner of all balances in the Drafts Payable Account and in the general account even at a time when it was, of course,

aware of the fact that conflicting claims would, no doubt, be advanced in view of the bankruptcy proceeding.*

Irrespective of this, however, the rights of the parties were fixed as of the date of the filing of the petition in bankruptcy. It has been shown that on that date no trust had been created, nor had the money in the Drafts Payable Account been equitably assigned, but on the contrary remained the property of and subject to the control of K. N. & K. The fact that control, which carried with it the ability to transfer, remained in K. N. & K., establishes that power in the bankrupts which is referred to in Section 70-a (3) and (5) of the Bankruptcy Act, and resulted in the Trustee's getting title to all of the balances with the B. C. I., including those credited to the Drafts Payable Account *as of the date of the filing of the petition in bankruptcy.*

*Everett* vs. *Judson*, 228 U. S., 474;
*Fairbanks Shovel Co.* vs. *Wills*, 240 U. S., 642, 649.

These were balances which the bankrupts "could by any means have transferred" and they accordingly were property owned by the bankrupts at the time of filing the petition which vested in the trustee in bankruptcy in pursuance of subdivision a(5) of Section 70 of the Act.†

*It already has been noted that the foreign bank involved in the *Zimmerman & Forshay* bankruptcy, 14 Fed. (2) 527, also returned balances credited to a Drafts Payable Account.

†Section 70 of the Bankruptcy Act provides:

"(a) The trustee of the estate of a bankrupt, upon his appointment and qualification, and his successor or successors, if he shall have one or more, upon his or their appointment and qualification, shall in turn be vested by operation of law with the title of the bankrupt, as of the date he was adjudged a bankrupt * * * to all * * * (3) powers which he might have exercised for his own benefit, but not those which he might have exercised for some other person; * * * (5) property which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him * * *."

By Section 47-a (2) of the Bankruptcy Act, the trustee is endowed with the rights and remedies of a creditor, "armed with process." He has all the rights of an attaching or levying creditor and clearly the fund in the B. C. I. could have been attached prior to the bankruptcy by any creditor of K. N. & K., just as in the *Eastman Kodak* case, *supra*, p. 19.

The life insurance cases holding that, where an assured reserves the right to change the beneficiary, the surrender value of the policy passed to the assured's trustee in bankruptcy and that the beneficiary named in the policy has no rights, despite the fact that the beneficiary was not changed prior to bankruptcy, are the familiar cases interpreting the foregoing bankruptcy section.

> See *Cohen* vs. *Samuel* (1915), 245 U. S., 50.

## POINT IV.

**The general object of the Bankruptcy Laws is to afford equality among all creditors remaining unpaid at the date of the bankruptcy and in order to obtain equitable relief or to establish a right to specific funds, the Courts have been strict in demanding that the claimant's right be founded upon the clear intention of the parties without vagueness or uncertainty. The respondent here has failed to sustain that burden.**

In *Westinghouse Electric & Manufacturing Co.* vs. *Brooklyn Rapid Transit Company* (C. C. A., 2nd, 1920), 263 Fed., 532, 536, the Court said:

> "In order to obtain equitable relief, or to establish an equitable lien, the courts have been strict in demanding that, as a condition of such enforcement, the intention of the parties should be clearly found from the expression of their contractual relation as found in the contract, and it must appear that there is no vagueness or uncertainty as to the terms or substance of the agreement."

See also

> *In re Stiger* (C. C. A., 3rd, 1913), 209 Fed., 148, 155.

It is evident, therefore, that one claiming priority, a lien or title to a specific fund which has come into the possession of the trustee, has the burden of proving his prior rights in accordance with recognized legal principles.

Has this respondent established a right to reclaim founded "upon the clear intention of the parties without vagueness and uncertainty?"

**The Vagueness of Respondent's Case.**

The fact that throughout this proceeding the respondent has declined to indicate who it claimed to be the alleged assignee of the fund—itself or the payee of the draft—is alone most persuasive evidence of the absence of any definite contractual obligation to set up a fund in favor of anybody. If even with the aid of astute counsel, and before the lower Court spoke, the inland banks could not determine whom they claimed to be the equitable assignee, can it be said that the respondent's case is without "that vagueness or uncertainty" which is required to give it a preference over other creditors.

It hardly needs citation of authority at this late date to establish the proposition that the general object of

the bankruptcy laws is to afford equality among all creditors remaining unpaid at the date of the bankruptcy, and that in the distribution of a bankrupt estate, equality is equity.

*In re Tindal* (D. C. S. C., 1907), 155 Fed., 456;

*In re Fowble* (D. C. Md., 1914), 213 Fed., 676, 681.

## POINT V.

### In Conclusion.

In conclusion it is respectfully urged that the respondent, and indirectly the 200 other inland banks, have failed to show that they stand in any different position from any other ordinary creditors of the bankrupts who purchased drafts or cable transfers and have failed to show that it is entitled to be paid its claim in full to the detriment of the other creditors. It is further urged that it has failed to establish the existence of any trust or fiduciary relationship, or the assignment of any specific fund whatever. *The inland banks contracted upon the faith of the credit of K. N. & K. as did thousands of other creditors whose claims have been filed with the trustee. Neither in law or in equity are they entitled to preferential payment out of the assets here for distribution.* Equality is equity.

Finally, the following language of the New York Court of Appeals in the *Leguit* case, 230 N. Y., 415, 424, is peculiarly applicable:

> *"There were also many other claimants to the assets. To establish a rule that in a case like this*

*the plaintiff becomes a preferred creditor; that the transaction is in the nature of a trust, and that checks deposited with banks upon the purchase of credit are trust funds held for certain and specified purposes, is apt to lead to much confusion, especially when those who have developed this method of doing business into a well-established custom have never treated them as such."*

**The decree of the Circuit Court of Appeals should be reversed and the respondent's reclamation petition should be dismissed.**

Respectfully submitted,

GODFREY GOLDMARK,
Counsel for Trustee-Petitioner.

GODFREY GOLDMARK,
RALPH F. COLIN,
Of Counsel.

Supreme Court, U.
FILED
DEC 6 1927
CHARLES ELMORE CROPLEY
CLERK

# Supreme Court of the United States

OCTOBER TERM, 1927.
No. 130

THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy of KNAUTH, NACHOD & KUHNE,

*Petitioner,*

*against*

THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO,

*Respondent.*

## BRIEF FOR PETITIONER IN ANSWER TO BRIEF FILED BY FIDELITY TRUST COMPANY OF NEW YORK AS AMICUS CURIAE.

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Of Counsel.

# Supreme Court of the United States

OCTOBER TERM—1927.

| | |
|---|---|
| THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy of Knauth, Nachod & Kuhne, Petitioner, *against* THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO, Respondent. | No. 130 |

## BRIEF FOR PETITIONER IN ANSWER TO BRIEF FILED BY THE FIDELITY TRUST COMPANY OF NEW YORK AS AMICUS CURIAE.

The Fidelity Trust Company of New York by leave of this Court has filed a brief *amicus curiae* in which it seeks to sustain the conclusions of the court below, but because of the necessities of its case, seeks to sustain those conclusions upon grounds different from those advanced by the Circuit Court of Appeals and different from those urged by respondent.

The facts with respect to the reclamation claim of the Fidelity Trust Company differ from those with respect to the Trinidad Bank claim, in that the English bank upon which the Fidelity Company drew its draft, unlike the Italian Bank, did not debit the amount of the

draft to K. N. & K.'s account when receiving the latter's advice of the drawing and did not maintain a "Drafts Payable Account," to which it would credit drafts advised but not yet presented. The English bank, it appears, only debited K. N. & K.'s account upon the presentation and payment of the draft. Being unable, therefore, to advance the argument that the charging of the advised draft to K. N. & K.'s general balance and crediting it to the omnibus Drafts Payable Account constituted an equitable assignment, the Fidelity Trust Co. is driven to advance the following arguments:

(1) That the mere mailing of the advice by K. N. & K. of the drawing of the draft by Fidelity Trust Co. and the mere acknowledgment of that advice by the English Bank constituted an irrevocable appropriation or assignment of an aliquot portion of K. N. & K.'s foreign balance which by some means this claimant will trace into the hands of the Trustee in Bankruptcy; that the book entries abroad were not essential to the completeness of the equitable assignment; and that the existence of an assignment or trust depended upon the acts of the parties to the Drawing Service and not that of the foreign bank.

(2) That the draft, or more properly speaking, the check, drawn by the Fidelity Trust Co. which directed a foreign bank "to pay from balance against this check" since it was drawn under K. N. & K.'s protection—itself constituted an assignment by K. N. & K. of a part of K. N. & K.'s deposit with the foreign bank.

(3) That the American dollars paid to K. N. & K. by the Fidelity Trust Company were to be applied to a particular purpose and were received initially and held in a fiduciary capacity.

## POINT I.

**The mailing of the advice by K. N. & K. of the drawing of the draft by Fidelity Trust Company did not constitute an irrevocable appropriation by K. N. & K. of any res which has come into the possession of the trustee.**

The sending of a letter of advice or letter of instructions is the usual practice in connection with the drawing of drafts and checks in international banking.

*Eastman Kodak Co.* vs. *National Park Bank*, 231 Fed. 320, affirmed no opinion (C. C. A. 2nd) 247 Fed. 1002;

*Beecher* vs. *Cosmopolitan Trust Co.*, 239 Mass. 48;

*Hopkinson* vs. *Forster*, L. R. 19 Eq. 74.

In the *Eastman Kodak* case and in *Hopkinson* vs. *Foster*, it was held that the advice did not constitute an assignment of any fund, and in the *Beecher* case the fact that there was such an advice was ignored in denying recovery. In the *Eastman Kodak* case, a draft or check was drawn upon a balance in the National Park Bank in New York and on the same day that the check was drawn, the foreign depositor sent a letter to the Park Bank which read as follows:

**Dear Sirs:**
**Please protect our checks for**
**$75.00—c o American Electric Railway Association.**
**$30,000.00—c o Bankers Trust Company a c Eastman Kodak Company.**

---

**$30,075.00 by the debit of our account."**

Before the check was paid, the drawer's balance in the Park Bank was attached. The drawer then went into bankruptcy and the holder of the draft claimed that the attachment must fail because the funds of the drawer to the amount of the advised check was a trust fund which had been equitably assigned, and, was therefore not subject to attachment. This argument was rejected and the general rule applied that the check itself did not constitute an assignment of the fund—and that the letter of advice did not change the result. Judge Learned Hand said:

> "Courts have no doubt often gone to some lengths to interpret the surrounding circumstances as indicating an agreement to assign, but in no case like this, when *the check was neither upon a specific fund nor for the whole amount of the fund*. The only facts to change the rule are that simultaneously with the check went an advice to the drawee as follows: 'Please protect our checks for $30,000 c/o Bankers Trust Co. a/c Eastman Kodak Co. by the debit of our account.' This is no more than the *common letter of advice* which frequently goes along with a foreign check; *it does not create an assignment*. *Aetna National Bank* vs. *Fourth National Bank*, 46 N. Y., 82, 7 Am. Rep. 314; *Hopkinson* vs. *Forster*, L. R. 19 Eq. 74. This is indeed alleged to have been the usual practice between the parties, and as such it cannot well have been meant to create an assignment. If so, the bank would at its peril have been obliged to keep a list of the advices in the order of their priority. To have paid out a later check, when advice had been received of the issuance of an earlier check, would have exposed the bank to a suit unless the account was good for all. No bank would consider a customer's business which was to be done in such terms. It pays checks as they are presented, and receives advices in the case of foreign depositors only for the purpose of identifying the items as they arrive. They serve

as a safeguard to the validity of the paper when the business is done at long range * * *.

"I think it an extremely pernicious thing to throw doubt upon the scope of doctrines governing negotiable paper which, though a mere skeleton of expression, is among the most useful inventions of mankind. *To seek too readily for exceptions from the well settled rules upon this branch of the law in pursuit of a supposed equity, which incidentally does not exist here, is an evidence of insufficient understanding of the economics of finance and their immense value to industry.*"

The Fidelity Trust Company attempts to avoid the obviously sound conclusion reached in the *Eastman Kodak* case by pointing out an alleged distinction in fact, namely, that in the present case the draft was drawn by the Fidelity Trust Company and the advice abroad was by K. N. & K. in pursuance of a contract. That is, it is argued, that although concededly the mere sending of an advice of the drawing of a draft does not effect an assignment or an irrevocable appropriation, the sending of such advice pursuant to a contract *does* constitute such an assignment or irrevocable appropriation.

It is to be noted that the form of advice sent in connection with Trinidad's draft and presumably in connection with the Fidelity Trust Company's draft was in the same form as that sent in the *Eastman Kodak* case quoted above, and the same as the form used by K. N. & K. to advise drafts drawn by "ourselves" (Ex. 6A, p. 164), namely, to "protect" the checks "to the debit" of the customer's account. The argument of the Fidelity Trust Company therefore amounts to this: If A draws his own draft upon his foreign correspondent and instructs that foreign correspondent to "protect" or "honor" the draft to the debit of the customer's account, there is no irrevocable appropriation. But if A

has contracted to "protect" or provide "sufficient funds" for the payment upon presentation of the drafts drawn by B and then advises his—A's—correspondent in precisely the same language as in the case of the drawing of A's own draft to protect or honor B's draft to the debit of A's account, the latter constitutes an equitable assignment or irrevocable appropriation

*There can be no such distinction.* The effect of the advice is just the same. A's obligation is the same in a case where he is the drawer of the draft as it is in the case where by virtue of contract he has agreed to protect the draft drawn by some third person. If the mere instructions to pay and debit are not an appropriation in one case, they are not in the other.

In each case the advice is "a mere letter of instructions to the bankers" (*Hopkinson* vs. *Forster*, *supra*)—in the one case to pay A's draft to the debit of A's account; in the other case to pay B's draft to the debit of A's account.

## No res Ever Existed.

Irrespective of the foregoing, it has not been made clear what "fund" was irrevocably appropriated and held in trust and eventually came into the possession of the Trustee. It is the well settled rule of this Court, as it is in England, that for a reclaimant to succeed, he must identify specifically the property which he claims and trace that specific property or fund into the Receiver's or Trustee's possession.

*Cunningham* vs. *Brown* (1924), 256 U. S., 1, 11;

*Duel* vs. *Hollins* (1916), 241 U. S., 523;

*Schuyler* vs. *Littlefield* (1914), 232 U. S., 707;

*In re Wait* (1927), 1 L. R. Ch. Div., 606.

And further, it is well settled that there can be no trust in or irrevocable appropriation of an aliquot share of a large fund. A reclaimant may only recover by showing the specific property which he claims is his. As Judge Holmes said in *National City Bank* vs. *Hotchkiss* (1913), 231 U. S., 50, at page 57:

> "A trust cannot be established in an aliquot share of a man's whole property, as distinguished from a particular fund, by showing that trust moneys have gone into it."

Because of the impossibility of tracing a *res*, if for no other reason, claims arising from circumstances such as those set forth in the brief of the Fidelity Trust Company cannot be allowed. There can be no trust or appropriation recognized if there is not in existence a fund held in trust or a fund appropriated.

## POINT II.

**The fact that the draft or check drawn by the Fidelity Trust Co. directed the foreign bank "to pay from balance against this check" did not result in an equitable assignment or appropriation of a portion of K. N. & K.'s balance with the foreign bank.**

The lengths to which the Fidelity Trust Company must go in order to sustain its argument and the efforts which are made to avoid the legal effect of the well established banking terms and practices are evidenced by its discussion as to the effect of the words used in the check.

Even the respondent in what must be deemed an exhaustive brief of 121 pages has failed, however, to advance the "argument" here made by the *amicus curiae*. If the argument is understood, it seems to be that the check was not a negotiable instrument because payable out of a particular fund; that, accordingly, it was an equitable assignment; that the Fidelity Trust Company had no balance in the foreign bank either at the time of the drawing of the check or at any other time and that, therefore, the check must constitute an assignment of *K. N. & K.'s* balance in the foreign bank.

The reason for the use of the words "pay from balance against this check" was of course that it was desired that the instruments to be drawn by the inland banks should be considered abroad as "checks" and not "drafts."

In continental Europe, there is a well recognized distinction between "checks" and "drafts." Checks are not subject to the same stamp taxes as are drafts. The identifying feature of a check is that it *purports* to be drawn upon a balance. Accordingly, the forms which K. N. & K. furnished to its innumerable inland customers throughout the country were drawn in the form considered as "checks" in international transactions. The checks were blank checks and the particular country upon which the particular inland bank would draw the check was unknown and therefore a form was provided which would be deemed a "check" in any country.

In *American Trust Company* vs. *Cosmopolitan Trust Company*, 239 Mass., 249, it appears that a check was drawn by the Cosmopolitan Trust Company "against our balance" in an Italian bank. There there was no question of a drawing service and yet this form was used. The check in that case read as follows:

"2514

Boston, Mass. U. S. A.

Lit 2 000 000

August Thirty First 1920

Against our balance

Pay to the Order of American Express Company

Duplicate being unpaid

The sum of Two Million lire

Cosmopolitan Trust Company

(sgd) W. W. Henderson

Assistant Manager.

Foreign Department.

To Credito Italiano

Genoa

Italy

No. 25846

That the distinction between the form of check and draft was evidently the reason for the form of the check here involved appears from the following authorities:

In the *Commercial Laws of the World*, Vol. 25, page 475, for example, there appears a summary of the development of the use of checks in the German Empire,* and it there appears that in order to develop the use of checks as distinguished from bills of exchange, checks at an early date were declared exempt from stamp tax. It also appears that in 1908, there was passed a German check law, which provided that the check must contain a direction addressed by the drawer or the drawee to pay a sum out of his property. But in discussing the effect of the provision the Article referred to states at page 478 that the requirements are merely of a formal nature and that the validity of the check does not depend

*That it was contemplated that checks would be drawn on Germany appears at fols. 425 and 432 and of course from the long list of German correspondents in Exhibit 1.

upon the drawer *actually having* a credit with the bank drawn upon. It is stated that it is the *form* of the check which is important in order to get the benefit of exemption from stamp duty. That all continental Europe recognizes a distinction is pointed out in *Chalmers, Bills of Exchange* (8th Ed., p. 285).

Finally the foregoing is confirmed by the following: In the League of Nations Document containing the Reports on the "Unification of Laws Relating to Bills of Exchange and Promissory Notes" there is included the individual report of Sir MacKenzie D. Chalmers, the British *rapporteur* and the author of "Chalmers on Bills" in which he says, page 99:

> "The Continental view of the function of bills and cheques differs fundamentally from the Anglo-American system. On the Continent a bill of exchange is merely an instrument of settling commercial debts. Finance bills are apparently not recognized. *The cheque is not a bill of exchange, but is an instrument sui generis.*"

This statement is supported by the discussion at page 58 of the same publication.

Even under our system certain courts have said that in order to constitute the draft a check it must purport to be drawn upon a deposit in a banker's hands. On this subject, 2 *Daniel, Negotiable Instruments* (6th Ed. Sec. 1569) says:

> "Sec. 1569. Thirdly. A check purports to be drawn upon a deposit. It is frequently said that a check is drawn upon a deposit in the banker's hands; and the fact that it is so drawn has been held necessary to constitute the draft a check. But this cannot be the true criterion. *It is not the fact that the order is actually drawn on a deposit, but the fact that it purports to be so drawn, which constitutes it a check; and it is more accurate to say that it is upon its face a draft upon a deposit.* To

> hold otherwise would authorize the construction of a written contract by the light of an extraneous fact of which the holder had no notice. If there were no deposit, it would be a fraudulent check—but a check, nevertheless—and we cannot conceive of a wider departure from principle than to hold that the fraud varied the nature of the instrument itself."

In view of the foregoing, it can hardly be seriously argued that because of the form of this check, it constituted an assignment by the inland banks of a portion of K. N. & K.'s balance in the foreign bank. The purpose of the transaction is obvious. The parties desired to use the form which would avoid stamp tax. The inland bank knew that it had contracted with K. N. & K. for the protection of the check. It had sufficient reason to believe that the check, because of this agreement, would be paid upon its presentation. It was justified, therefore, in drawing the check, which purported to be drawn upon a balance despite the fact that it, the inland bank, had no balance with the foreign bank and in fact had no contractual relations with it.

## POINT III.

**The American Dollars were not paid to K. N. & K. by the Fidelity Trust Company to be applied to a particular purpose and to be received and held in a fiduciary capacity.**

The argument in support of this contention has already been set forth at length in the petitioner's principal brief. The recent cases dealing with foreign ex-

change transactions clearly indicate that the courts are unwilling to hamper foreign banking transactions and to impose a trust relationship where in fact none was contemplated and where reliance was placed upon the general credit of the international banker.

The case of *Farley* vs. *Turner*, 26 L. J. Ch., 710, to which reference has been made is not an authority to the contrary, for it is essentially different in its facts from the case at bar. In that case, Goodwin paid to his bankers, Farley, Turner & Jones, £707 with directions that £500 of that money was to be paid to Robarts & Co., another firm of bankers, to meet an acceptance of Goodwin, payable at Robarts & Co. Farley, Turner & Jones then sent certain bills of exchange to third parties and directed that the proceeds thereof be paid to Robarts & Co. for the express purpose of taking up Goodwin's draft. This was done but before it was taken up, one of the partners of Farley, Turner & Jones died and Robarts returned the £500 to the legal representative of the firm. The question was whether this £500 belonged to Goodwin or to the general creditors of Farley, Turner & Jones. The Court held the money had been received by Farley, Turner & Jones to be applied to a particular purpose, and that they in turn had paid the money to Robarts to be applied to a particular purpose, and that, therefore, when the money was not applied to that purpose but was returned, it belonged not to the general creditors but to Goodwin who had paid it for a particular purpose.

It is, of course, to be noted that in that case, Farley, Turner & Jones did not have a general account with Robarts to the debit of which Robarts was directed to pay Goodwin's draft. In that case the Farley firm had not received a consideration from its customer for its service in having the customer's acceptance paid to the debit of the Farley firm's account. It was not held that

the Farley firm had given such directions for the payment of the draft as amounted to an irrevocable appropriation of or an equitable assignment of any of *their general balance*, nor was it held that entries made in Robarts' books constituted an assignment of any of Farley's balance. Nor did that case involve the consideration of the purpose or legal effect of the crediting to a Drafts Payable Account in accordance with international banking practices. It did not involve a foreign exchange transaction or an agreement to provide a credit in foreign currency, which transactions under modern authorities are held to be merely executory contracts for the sale of credit. The case, of course, did not involve the construction of the provisions of a "drawing service" under which innumerable checks are being drawn and advised each day. The case simply held that the Farley firm was merely a conduit for carrying the fund deposited with it by Goodwin to Robarts to meet Goodwin's acceptance. That acceptance was not be paid from any balance belonging to Farley or to the debit of any credit ever owned by Farley. Farley had no absolute obligation toward Goodwin to provide "sufficient funds" to pay the acceptance nor to "protect" it. Farley's sole obligation was to forward the amount deposited by Goodwin. If it were not sufficient to pay the acceptance, there would have been no further obligation on Farley.

Finally, it did not involve the construction of Section 70 of the Bankruptcy Law which vests in the Trustee in Bankruptcy title to all property which the bankrupts could have transferred or over which they had the power of distribution. *Farley* vs. *Turner* involve an isolated transaction where a specific sum was paid for a specific purpose and where the sum thus paid was forwarded with specific instructions to take up a specific draft. The principle underlying it

cannot aid in construing the drawing service, or the purpose or effect of a Drafts Payable Account and the reserved right of cancellation.

## CONCLUSION.

The additional argument made by the Fidelity Trust Company, as *amicus curiae*, simply emphasizes the complications which result from the contention that mere instructions from K. N & K. to their foreign correspondent to protect the draft to the debit of K. N. & K.'s account and the entries in the Drafts Payable Account made anyone other than K. N. & K. a creditor of the foreign bank until the draft was paid. It shows how far-fetched are the arguments advanced in this case to obtain an advantage over the general creditors, all of whom trusted the credit of K. N. & K. By the use of such terms as "balances", "funds" and "transmission," it is sought to obscure what is in its essence a very simple, ordinary banking transaction, namely, the protection by B of the draft of A—the payment of A's draft from B's credit. The conflicting arguments of the respondent and of the *amicus curiae*—the one relying on the "Drafts Payable Account" and the other asserting it to be immaterial—result only in establishing the soundness of the petitioner's interpretation of the fundamental relations of the parties, namely:

That K. N. & K. were acting as *entrepreneurs* who, for a consideration, undertook for American dollars paid in advance that they would have a sufficient credit with the foreign drawee bank upon the presentation of the check drawn by the inland bank, so that the check would be paid to the debit of K. N. & K.'s balance in pursuance of ordi-

nary banking practices and in the same manner as checks drawn by K. N. & K. themselves. For reasons already set forth, until presentation and payment of the checks, the balances in the Drafts Payable Account in law and in equity were subject to the control of K. N. & K. and therefore passed to petitioner as Trustee in Bankruptcy.

Respectfully submitted,

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RALPH F. COLIN,
Of Counsel.

Office Supreme Court,
FILED
OCT 18 1926
WM. R. STANSBURY
CLERK

No. 130

# Supreme Court of the United States

**October Term—1926**

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THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy of Knauth, Nachod & Kuhne,

*Petitioner,*

*against*

THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO,

*Respondent.*

## BRIEF OF RESPONDENT IN OPPOSITION TO PETITIONER'S APPLICATION FOR A WRIT OF CERTIORARI

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## Subject Index


PAGE

Statement of the case and the questions involved ... 1

The Trustee's reliance upon a contention unsupported by the record and contrary to the uncontradicted evidence ... 3

The *Modus Operandi* of the Drawing Service ... 6

Terms and conditions of the Drawing Service ... 7

Facts ... 9

Brief of the Argument ... 18

POINT I.

Pursuant to the terms of the Drawing Service, the bankrupts caused Banca Commerciale Italiana to create, out of the bankrupts' funds on deposit with Banca Commerciale Italiana, a fund for the payment of the draft involved in this proceeding. Thereby an equitable assignment of the moneys was effected ... 19

POINT II.

Moneys remitted to the bankrupts in connection with the drawing of a draft under the terms and provisions of the bankrupts' Drawing Service were received by the bankrupts as agents of the remitter for the purpose of applying the same to the payment of the draft ... 36

POINT III.

The petition for a Writ of Certiorari should be denied ... 50

## Table of Authorities


| | PAGE |
|---|---|
| American & English Encyclopedia of Law, Sec. Ed., Vol. 19, p. 16 | 28 |
| Burdett v. Willett, 2 Vernon, 638 | 40 |
| Burns v. Carvalho, 4 W. & C. 890 | 24 |
| City of St. Louis v. Johnson, 5 Dillon 241 | 40 |
| Coates v. First National Bank of Emporia, 91 N. Y. 20 | 21 |
| Corpus Juris, Vol. 8, pages 83-372-831-1004 | 32 |
| Cutler v. Am. Ex. Natl. Bank, 113 N. Y. 593 | 32, 40 |
| Equitable Trust Co. v. Keene, 232 N. Y. 290, 295 | 44 |
| Farley v. Turner, 26 L. J. Ch. 710 | 38 |
| Fortier v. Delgado & Co., 122 Fed. 604 | 21 |
| Fourth St. National Bank v. Yardley, 165 U. S. 634 | 21 |
| Giles v. Perkins, 9 East. 12 | 40 |
| Hackett v. Campbell, 10 App. Div. (N. Y.) 523 | 21 |
| In re A. Bolognesi & Co., 254 Fed. Rep. 770 | 40 |
| In re Jarmulowsky, 258 Fed. Rep. 231 | 40 |
| Kingman v. Hotaling, 25 Wend. 423 | 32 |
| Massey v. Fisher, 62 Fed. Rep. 958 | 40 |
| Moreland v. Brown, 86 Fed. Rep. 257 | 40 |
| Muller v. Kling, 209 N. Y. 239 | 21 |
| Peak v. Ellicott, 30 Kansas 156, 1 Pac. Rep. 499 | 40 |
| People v. City Bank of Rochester, 96 N. Y. 32 | 40 |
| People ex rel Zotti v. Flynn, 135 App. Div. 276 | 40 |
| Risley v. Phoenix Bank, 83 N. Y. 318 | 21 |
| Rivers v. A. & C. Wright Co., 43 Southeastern 499 | 21 |
| Roca v. Byrne, 145 N. Y. 182 | 40 |
| Ryan v. Phillips, 3 Kans. App. 768 44 Pac. Rep. 909 | 40 |
| Star Cutter Co. v. Smith, 37 Ill. App. 212 | 40 |
| Throop Grain Cleaner v. Smith, 110 N. Y. 83 | 21 |


### Official Report of the Opinion Delivered in the Court Below

In re Gubelman, et al., ex parte First National Bank of Trinidad, 13 Fed. Rep. (2nd Series) 732.

# Supreme Court of the United States

**October Term—1926.**

THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy of Knauth, Nachod & Kuhne,

*Petitioner,*

*against*

THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO,

*Respondent.*

## *BRIEF OF RESPONDENT IN OPPOSITION TO PETITIONER'S APPLICATION FOR A WRIT OF CERTIORARI.*

(Italics Ours)

### *Statement of the Case.*

Knauth, Nachod & Kuhne, a partnership, was petitioned in Bankruptcy in the Southern District of New York on June 15, 1923, and thereafter, in due course, a Trustee in Bankruptcy was elected.

Up to the time of the Bankruptcy, Knauth, Nachod & Kuhne (which for convenience will hereafter be referred to as K., N. & K.) were Commercial Bankers. In the course of their business they conducted, for profit, what was known as a "Drawing Service," the operation of which will be described presently, and solicited inland

banks to deal with them under it. The claimant availed itself of the "Drawing Service" and, in accordance with the terms thereof, sold to its customer its draft on K., N. & K.'s Italian correspondent, Banca Commerciale Italiana (hereinafter called B. C. I.) at Sassari, Italy, and thereupon forwarded certain monies to K., N. & K. K., N. & K. thereupon had certain transactions with B. C. I., its correspondent, and out of these circumstances two questions were presented by the claimant's reclamation petition. Tersely stated these questions are:

(1) Did the Bankrupts receive claimant's remittance as claimant's agents, to apply the same to a particular purpose?

(2) Independently of (1), was there an equitable assignment by the Bankrupts of certain monies, on deposit by them with B. C. I., for the payment of the draft involved in this proceeding?

The learned Special Master, to whom the petition was referred, decided both questions in the negative. Upon the Trustee's motion, the Special Master's report was confirmed in the District Court, with an opinion in which the learned Judge said (fol. 669):

> "The law finally to be applied to the subject matter of this controversy between claimant and Trustee in Bankruptcy of K. N. & K. will be declared by the Appellate Court and my views concerning the same are of fleeting importance * * *."

Upon appeal to the United States Circuit Court of Appeals for the Second Circuit, the order of the District Court was reversed and the reclamation claim allowed,

the Circuit Court of Appeals finding that there had been an equitable assignment for claimant's benefit and finding it unnecessary to pass upon the question whether the monies were originally transmitted to the Bankrupts for a particular purpose (fol. 769). The opinion of the Circuit Court of Appeals is reported in 13 Fed. (2nd Series) page 732.

The Trustee in Bankruptcy contends that the conclusion of the Circuit Court of Appeals was erroneous. His claim is summarized in his statement of "The Contentions of Petitioner-Trustee" (Petition, pp. 4-5) and appears to be predicated solely upon the claim that there could not have been an equitable assignment, "because they (K., N. & K.) retained control of the amount so credited"—referring to the monies which the Circuit Court held had been equitably assigned.

*It is a singular circumstance and, considering the emphasis which was placed upon the fact in the Courts below, an omission which cannot be attributed to inadvertence alone, that the Trustee persists in ignoring, if not suppressing, in his statement of the facts and his quotations from the testimony, the uncontradicted testimony of his own witnesses, that the Bankrupts did* NOT *retain* [redacted] *the control which counsel asserts as the basis for his argument.*

This alleged control is the foundation of the Trustee's contention. There is no dispute in the testimony about the fact that no such control existed, and only the weakness of the Trustee's position can explain this attempt to create an impression unsupported by the Record and contrary to the uncontradicted testimony of his own witnesses.

It may reduce the labor of the Court if we dispose of this question at the outset, and we shall, therefore, though it be at a risk of sacrificing logical sequence, direct the Court's attention to the evidence which will dispel any doubt that may remain upon the subject.

Mr. Dawson, the Trustee's expert on international banking, was asked (fol. 350):

> "Is there * * * a general practice or custom with respect to the cancellation of advices after their receipt by a foreign bank and prior to the presentation of a draft for payment."

He was very cautious in his answer. First he asked to have the question repeated; after he heard it the second time he answered (fol. 351): "There is a custom." He was then asked:

> "What is that custom?"

and he replied (fol. 351):

> "*I take it the question means when the drawer bank wants to cancel a draft that has already been drawn and advised,*"

and Mr. Goldmark, the learned counsel for the Trustee, who was examining, said (fol. 352):

> "Precisely."

Thus it appears that the question put to Dawson, as limited by him with the concurrence of counsel, was:

> "Is there a general practice or custom with respect to the cancellation of advices after their receipt by a foreign bank and prior to the presentation of a draft for payment *where the drawer bank wants to cancel a draft that has already been advised?*"

The Court will observe that this was not such a case. *The drawer bank here was the claimant—not K., N. & K.* It is conceded that the claimant did not want to cancel the draft it had drawn and which K., N. & K. had advised abroad. Consequently, the testimony of Dawson that in cases where

> "the drawer bank wants to cancel a draft that has already been drawn and advised"

K., N. & K. would have the right to send notice of cancellation to the foreign bank, and the foreign bank would recognize such notices, has absolutely nothing to do with this case. Dawson was very careful to limit his statement of the custom so that it did not apply to the facts of this case. Yet it is this answer by Dawson (fol. 352), *and this answer alone*, upon which the Trustee builds his argument that the Bankrupts retained control of the fund in the hands of B. C. I. and that there could not, therefore, have been an equitable assignment. Obviously, the foundation does not exist and the argument is baseless.

K., N. & K. also recognized that it was authorized to cancel drafts previously advised *only in cases where the drawer bank requested it to do so.* This appears from the fact that it is undisputed that K., N. & K. never attempted to exercise such a right *except in cases where they had first been advised by the drawer bank that the draft had been lost or would not be presented to the drawee bank for payment* (fols. 282-284).

We believe the foregoing discussion of Dawson's testimony, even though it be slightly out of its logical order, may facilitate the disposition of this matter by the Court by disposing at the outset of the baseless state-

ments, iterated and reiterated in petitioner's brief, that K., N. & K. retained control over moneys taken from its account and credited to the "Drafts Payable" account. We now proceed to a more detailed statement of the facts and a discussion of the law applicable thereto.

### *The Modus Operandi of the Drawing Service.*

The bankrupts supplied their inland correspondents (of which claimant was one) with a list of their foreign correspondents (Claimant's Exhibit "1," fols. 418-473) and a printed book of "Foreign Drafts" (Claimant's Exhibit "2," fols. 473-480). Each page in the book of "Foreign Drafts" contained two forms, the upper a blank draft (fol. 478), and the lower, an "Advice." The pages were perforated, so that these forms could be detached from the book and also separated from each other. When a customer of an inland bank sought a draft payable abroad, the bank would consult the "rate card" issued by the Bankrupts, on which the Bankrupts stated the rates at which they would "protect" drafts drawn that day on their various foreign correspondents. Thereupon, in return for an amount fixed on the basis of such rate, the inland bank, using one of the forms in the book of "Foreign Drafts," would issue to its customer *its own draft* on one of the correspondents listed by Bankrupts in their "Drawing Service." The bank would then fill out an "Advice" contained in the book of "Foreign Drafts," detach it from the book and immediately mail it to the Bankrupts with sufficient funds, computed at the rate fixed by the Bankrupts in their Rate Card for the drawing of the draft on that day.

### *Terms and Conditions of Drawing Service.*

In the "Drawing Service" we find the following provision under the title "Terms and Conditions Governing the Use of K., N. & K. Drawing Service (fols. 422-423):

> "Upon receipt of advice by draft, accompanied by adequate funds payable at par in New York, we shall promptly forward our advice of the same and provide the drawee with funds sufficient for the payment of the draft abroad, by a transfer of credit from our balance, or otherwise, provided the draft is drawn on a bank named in our latest list of correspondents.
>
> *Under this arrangement, our correspondents in this country act as principals, and issue drafts in their own names, our name not appearing thereon. In other words, we are employed merely as the* AGENTS *of the drawers for the purpose of advising the issue of their drafts and providing the drawee banks with sufficient funds to cover their payment.*"

On the cover of the book of "Foreign Drafts," the relationship of principal and agent is again emphasized (fols. 474-475):

> "Upon receipt of advice of draft accompanied by adequate funds payable at par in New York, we shall promptly forward our advice of same, and make provision for its payment abroad, provided it is drawn on a bank named in our latest list of correspondents.
>
> *Under this arrangement our correspondents draw drafts for their own account as principals and our name does not appear,* OUR SOLE FUNCTION BEING TO ADVISE THE DRAWEES OF THE ISSUE OF DRAFTS

DRAWN BY OUR CORRESPONDENTS AND TO PROVIDE FOR PAYMENT, IN WHICH FUNCTION WE ACT AS AGENTS OF THE DRAWERS."

To make assurance doubly sure and to estop the inland bank from ever contending that the money had been sent to K., N. & K. in any capacity other than as agent to transfer it abroad, we find K., N. & K. printing into the stub, which would remain with the inland bank as the "Issuing Bank's Record" of the transaction, the words (fol. 480) "Paid K., N. & K. * * * (*Transfer Agents*)".

We must bear in mind that the language of the Drawing Service was chosen by the Bankrupts and that at the time they drew the Drawing Service they were contracting upon the theory they would continue in business and they were protecting themselves accordingly. They wanted no doubt or misunderstanding about the fact that for the negligible fee they received in connection with drafts drawn under the Drawing Service they were not guarantors of the continued solvency of every one of the thousands of banks throughout Europe upon which drafts might be drawn. They undertook to provide a fund abroad and they wanted it perfectly clear that once they did that their obligation was met and their liability ended. If thereafter the foreign bank should become insolvent, or for some other reason fail to honor the draft, K., N. & K. did not propose to answer for such defaults. It would be difficult to choose language better adapted to their purpose. They state and reiterate throughout the Drawing Service that they are employed merely as the "*agents*" of the drawers for the purpose of advising the issue of their drafts and providing the drawee bank with sufficient

funds to cover their payment, and to dispel the last shred of doubt they create an estoppel by making the inland bank's own record of the transaction show that it sent the money to K., N. & K. as "*transfer agents.*"

The draft and the "Advice" involved in this proceeding are Claimant's Exhibits "3" and "4" (fols. 481-483). The draft was for 24,360 Lire, drawn by Claimant on Banca Commerciale Italiana, Sassari, Italy, in favor of Zara Sanna Giovanni.

The "Advice" mailed by Claimant to Bankrupts immediately upon the sale of the said draft reads (fols. 482 483):

> "Pursuant to the terms and conditions governing your drawing service we have sold draft, bearing the above number, dated Trinidad, Colo., May 19, 1923.
>
> For Lit. 24,360.00 and shall thank you to protect same upon presentation.
>
> We remit herewith the sum of 1,191.20 at rate 4 89 quoted on Rate Card No. 18."

Claimant's check for $1,191.21, which accompanied the "Advice," was received by the Bankrupts and deposited by them in their bank account. The draft was duly presented for payment but dishonored. The failure to pay the draft was not based upon any direction by Bankrupts to the foreign bank nor was it based on any failure on their part to actually create the fund with which to pay the draft. *They did create this fund and they made no attempt to destroy it or withdraw it. It remained with the foreign bank until the Receiver, long after bankruptcy but before the draft was presented, procured it to be sent to him.*

Immediately upon receipt of the claimant's "Advice" and the check to cover, the Bankrupts notified the Italian Bank of the drawing of the claimant's draft and directed the bank to "honor" it, "charging the same to our account," and in another communication, sent at the same time, directed the foreign bank to charge the said draft "to the debit of our account" (Claimant's Exhibit 6 and 6B; 6B being a recapitulation sent to the principal office of the B. C. I. of the drafts advised to its several branches, and 6D being the advice to the Sassari branch of the B. C. I. covering the draft involved in this proceeding. The court will note that the total of 6D, drafts drawn on the Sassari Branch, is included as one of the items on the recapitulation, Exhibit 6).

It is stipulated that the foregoing papers were received by B. C. I. on or before June 4, 1923 (fol. 76). They are known as Steamer Block "SS 8469-B." It is stipulated that there was a regular course of dealing between the B. C. I. and the Bankrupts, by which the B. C. I. sent to the Bankrupts, approximately each week, statements of the Bankrupts' account with the B. C. I. (fol. 78); that on these statements the B. C. I. showed that it had debited the Bankrupts' account with the amounts of drafts advised and that this practice of immediately debiting the Bankrupts' account with these amounts was recognized as proper by the Bankrupts (fols. 81, 82). Claimant's Exhibit 8 is one of these statements of account, from which it appears that on June 4, 1923, the bank abroad debited Bankrupts' account with the total of Steamer Block "SS 8469-B," which included claimant's draft, and that it reported to the Bankrupts that it carried forward for their account a specified balance, *which*

*remained after deducting from their former balance various sums, including the amount of Steamer Block "SS 8469-B."* Claimant's Exhibit 9, which is another of these statements, carrying the account up to and including the date of bankruptcy, shows that at no time up to and including this date did the bank abroad recredit to the Bankrupts any of the moneys which had been charged out of their account to cover Steamer Block "SS 8469-B."

Not only do the stipulated facts show that the money was taken *out of the Bankrupts' account*, but they go further and show that these moneys, upon being taken out of the Bankrupts' account, were *credited to an account maintained by the B. C. I. entitled "Drafts Payable,"*

> "in which account were also credited amounts of drafts advised to the said B. C. I. for payment by other depositors or clients of the B. C. I. in addition to the bankrupts" (fols. 89, 90).

No better statement of the nature and the purpose of the account to which these moneys were credited by the foreign bank could be made than that of the Trustee's witness, Mr. Dawson, Vice-President of the Guaranty Trust Company (fols. 339-340). Mr. Dawson said that he was familiar with the practices and usages in connection with the protection of drafts by New York bankers on behalf of inland banks (fols. 345-346); that there was a "universal custom" in this regard (fol. 348) pursuant to which

> "the drawee bank, upon receipt of advice from its client that a draft has been drawn on it, immediately charges the current account of that client with the amount of any draft or drafts and *sets it aside in a special fund awaiting the presentation of any drafts against that fund.*"

At folios 356-357 Mr. Dawson said that originally the drawee banker, upon receiving notice that a draft had been drawn on him,

> "*held the money in his box or in his office, useless, awaiting the presentation of the commitment or draft.*"

and (fol. 372)

> "probably earmarked each particular bag for a particular purpose";

further, that this practice (fol. 357)

> "has hung on in modern times • • • "

except that now the foreign bank accomplishes (fol. 365)

> "*exactly the same result*"

by making appropriate book entries, or, to put it another way (fol. 370):

> "We still keep the money in the box, but not specifically. We look over our active liabilities which are imminent, and readjust our cash position in general, but not specifically."

The Trustee shies perceptibly at this testimony of his own witness and seeks to minimize it by describing it as merely Mr. Dawson's "belief." It is characterized by the Trustee as fallacious because, says the Trustee,

> "The bankers in early days who are said to have set aside cash to meet advised drafts were not setting aside cash which belonged to their depositors, but *their own cash*, so that *they* would be in the 'possession of funds to meet their commitments.'" (Trustee's brief, p. 37; italics by Trustee).

We are unable to find any basis in the record for suspecting that the money which the banker set aside in the "early days" came from any source different from the money which the banker now sets aside. Of course, the banker "in early days" did not keep all of his deposits in cash. Neither does a banker today. The deposits were then converted into investments just as they are today. They are the property of the banker and he is merely a debtor of his depositor. The same was true "in early days." The point Mr. Dawson made was that in the early days, as soon as the foreign banker received notification that a draft had been drawn on him, the banker would "liquidate his investments" sufficiently to put himself in funds to meet the draft; put the money for each draft into a separate bag and (fol. 372) "probably earmarked each bag for a particular purpose" and "held (them) * * * in his box or in his office, useless, awaiting the presentation of the commitment or draft," and that "exactly the same result" is accomplished today by debiting the depositor and crediting "Drafts Payable," which is the banker's present name for "his box." Nowadays (fol. 356) with the existence of "banks of rediscount or methods of suddenly raising cash" it is not necessary actually to "liquidate" the investments but the same result is accomplished (fol. 365) by "book entries," or to put it in another way (fol. 370)

> "We still keep the money in the box, but not specifically. We look over our active liabilities which are imminent, and readjust our cash position in general, but not specifically."

Here is also a clear recognition that upon the receipt of an advice and the crediting of "Drafts Payable" the liability becomes "our liability," that is, *the liability of*

*the drawee bank*. That K., N. & K. clearly recognized this is corroborated by the fact that once K., N. & K. advised a draft abroad, they were not interested in whether the same was ever presented—it was no longer any concern of theirs (fol. 433).

The stipulated facts show further that although the Bankrupts were entitled to and did receive interest on their balance with the B. C. I., they recognized that they were not entitled to receive and did not receive interest on moneys deducted from their account and credited to the "Drafts Payable" account as a result of their advices of drafts drawn (fol. 92). The Trustee argues that the reason the foreign bank did not pay interest upon the moneys taken out of a depositor's account and put into the "Drafts Payable" account is that the use of the money

> "constituted the bank's compensation for its service in meeting the draft" (Brief, p. 33).

This statement is based upon the testimony of Dawson (fol. 357), that the original practice of the foreign banker of holding the money in his box, awaiting presentation of the commitment

> "has hung on in modern times like a great many other practices and has been availed of as a means frequently of compensating a banker for an account that would otherwise be troublesome and a loss. You have many accounts frequently that are active, which on bare balances in current accounts, are a lot of trouble and a loss in handling that would not be worth while and there is always a non interest bearing float that compensates you for the trouble you take."

This testimony of Dawson cannot be interpreted as suggesting that the *reason* for taking the money out of K., N. & K.'s account and putting it into the "Drafts Payable" account was that thereby it ceased drawing interest and thus indirectly provided "compensation" to the foreign bank for "the trouble" it took. It may very well be that the foreign bank, in determining whether or not it would handle this class of business, took into account the fact that it would result in providing the bank with funds free of interest charges, and that the foreign bank concluded that this circumstance made this class of business profitable. This, however, has nothing to do with the question whether, when the money was taken out of K., N. & K.'s account and put in the "Drafts Payable" account as "A special fund awaiting the presentation of any drafts drawn against that fund," there was, or was not, an equitable assignment. The question is not what considerations prompted the foreign bank to take on the business, but what the foreign bank did after it took on the business.

The stipulated facts show that while the fund was set apart and held by the bank abroad for the purpose of meeting the claimant's draft, the receiver cabled the bank abroad (Claimant's Exhibit 10) that "all credit balances in favor of Knauth, Nachod & Kuhne, New York, must be held subject to my sole order."

It is interesting to note the response which this cablegram elicited from B. C. I. (Claimant's Exhibit 11). They enclosed the statement (Claimant's Exhibit 9), showing the state of the Bankrupt's account up to the date of bankruptcy. This statement shows that the amount of Steamer Block "SS 8469-B" had been

charged out of the Bankrupts' account and had been credited to Drafts Payable on the books of B. C. I. *and that B. C. I. was indebted to the Bankrupts only in the sum which remained after deducting from the former credit balance of the Bankrupts, the amount of Steamer Block "SS 8469-B" and certain other Steamer Blocks advised by the Bankrupts.*

The next significant thing in Claimant's Exhibit 11 is B. C. I.'s notification to the Receiver that certain Steamer Blocks which had been advised by Bankrupts were (fols. 528-529)

> "being held in abeyance, not having been debited to the account *through lack of funds.*"

This establishes that even as between the parties themselves the charging of Bankrupts' account and the crediting of "Drafts Payable" were not mere "book entries," as the Trustee contends, *but were intended to record actual transfers of funds from one account to another.* On no other theory can the refusal of the B. C. I. to make the book entries on account of "lack of funds" be explained.

On June 29, 1923, the receiver wrote B. C. I. (Claimant's Exhibit 14) requesting it to

> "rule off the account" of Knauth, Nachod & Kuhne on June 16, 1923, and to forward to him by return mail "a statement of their account up to that date, *as well as* a list of all unexecuted cable transfers and unpaid drafts and money orders • • • ."

which again indicates that in the mind of the Receiver, when he sent this letter, "a statement of the bankrupt's account" on June 16, 1923, would *not* include moneys

which had been set aside by B. C. I. to meet drafts theretofore advised to it by Bankrupts.

On August 23, 1923, the receiver cabled B. C. I. (Claimant's Ex. 18) to

> "*cancel all drafts* charged but not paid before receivership and remit balance for (our) my credit to Central Union Trust Co., New York."

On September 10, 1923, B. C. I. wrote the receiver another important letter (Claimant's Exhibit 19).

In the first place it confirmed a letter sent to the receiver on September 8, 1923, which the Trustee has not produced.

In the second place it gave a resume of certain enclosures (Claimant's Exhibits 19A and 19B) showing the condition of the Bankrupt's account and explaining how the fund returned to the Receiver was made up.

Claimant's Exhibit 19B, one of the enclosures in Exhibit 19, was a statement showing a balance in the Bankrupt's favor of 1,629,770 lira. This statement and the letter in which it was enclosed show that in arriving at this balance B. C. I. had accepted the Receiver's direction to "cancel all drafts charged but not paid before receivership" and had thereupon recredited to the account of the Bankrupts the sum of 1,526,048.48 lira, *which sum represented certain specified amounts theretofore taken out of the Bankrupt's account and credited to Drafts Payable to meet drafts advised, when presented.* A detailed statement of the drafts, the amounts of which were so recredited, was also enclosed in this letter and is Claimant's Exhibit 19A. A reference to Exhibit 19A (fol. 560), shows that among these drafts *is draft 61161*

*drawn by this claimant on the Sassari office for 24,360 lira, being the draft which is the subject of this controversy.*

The testimony is undisputed that the Bankrupts had a right to cancel drafts advised *only in cases where the drawer bank first notified them that it desired to cancel the draft* and it is also undisputed that the Bankrupts had never assumed to exercise such a right *except in cases where they had first been advised by the drawer bank "That the draft had been lost or would not be presented to the drawee Bank for payment"* (fols. 282-284). There was no such notification in this case.

Whether, upon receipt of the Receiver's notification to "Cancel all drafts charged but not paid before receivership," the B. C. I. assumed that the receiver was within his rights, as between him and the drawer banks, need not now be considered. The fact is that the Receiver was *not* within his rights, and having, in violation of right, procured possession of the fund which had been set apart to pay these drafts, he is in no position to keep that fund as against the holders of the drafts.

It is stipulated that the amount shown on Claimant's Exhibit 19B was returned to the Receiver by the payment of its equivalent in dollars, to wit, $67,548.06 (fol. 111).

## Brief of the Argument.

The claimant contends:

I.

Equitable assignment is a matter of intention. The intention to create an equitable assignment, and the actual creation thereof, clearly appear from the undertakings of

the Bankrupts as set forth in the Drawing Service, followed by the Bankrupts' directions to their foreign correspondent and the acts of the foreign correspondent, with the knowledge and acquiescence of the Bankrupts, upon the foreign correspondent's receipt of the Bankrupts' directions.

II.

By the express terms of the Drawing Service the Bankrupts were merely the agents of the claimant to provide Banca Commerciale Italiana with moneys, supplied by the claimant, to meet the draft which claimant had drawn.

## POINT I.

**Pursuant to the terms of the drawing service, the Bankrupts caused Banca Commerciale Italiana to create, out of the Bankrupt's funds on deposit with Banca Commerciale Italiana, a fund for the payment of the draft involved in this proceeding. Thereby an equitable assignment of the moneys was effected.**

Equitable assignment is a matter of intention, to be determined from the circumstances of the case and the acts and declarations of the parties. If it appear that there is an intent on the part of a creditor to have his debtor set aside and appropriate, for the benefit of a third party, a portion of the funds of the creditor in the hands of the debtor, followed by some act of appropriation by the debtor at the creditor's request, an equitable assignment in favor of such third party takes place.

What more cogent proof could be presented than is stipulated in this case to show that K., N. & K. intended that B. C. I. should, and that B. C. I. in fact *did*, set aside, out of moneys of K., N. & K. in its hands, a sum for the payment of the draft here in controversy?

K., N. & K. notified B. C. I. that the draft had been drawn and directed B. C. I. to charge the same against its account and honor the draft when presented. B. C. I. did charge the account of K., N. & K. with the amount of the draft, and the amount so charged was taken out of K., N. & K.'s account and put into an account maintained by B. C. I. for the payment of drafts advised. This account included, as the stipulation admits, not only moneys appropriated for the payment of drafts drawn under the K., N. & K. Drawing Service, *but moneys appropriated for the payment of drafts drawn by others as well. The Bankrupts had no rights in the moneys in that account—they were held by the foreign bank "in a special fund" to accomplish "exactly the same result" as was originally accomplished by "earmarking each particular bag for a particular purpose" and putting it aside "in a box" to "await the presentation of the draft"* (fols. 348, 356-357, 369-370, 372). Once the money was taken out of K., N. & K.'s account, they ceased to receive interest on it, although they did receive interest on the moneys which *were* in their account.

In reporting to K., N. & K. with respect to the amount of its balance in its hands, B. C. I. showed K., N. & K., by its statements, that it did not treat as any part of K., N. & K.'s balance in its hands the moneys which had been taken out of the account and credited to the Drafts Payable account. This practice, it is stipulated, was proper.

Of course, if there had been an equitable assignment, *the money ceased to be the property of K., N. & K.*; K. N. & K. had no right to demand the return of it and its receiver had no greater right. The receiver did, with full knowledge of the facts, assume to take possession of this money, which did not belong to the Bankrupts, and which is, accordingly, no part of the bankrupt estate. The moneys returned are earmarked by the Exhibit which explains how they are arrived at and which shows that *they include the very moneys which had been set aside and were being held to pay the draft in controversy here.* The claimant as the holder of that draft is the owner of this money and is entitled to reclaim it.

*Coates* v. *First National Bank of Emporia*, 91 N. Y. 20;

*Risley* v. *Phoenix Bank*, 83 N. Y. 318;

*Throop Grain Cleaner Co.* v. *Smith*, 110 N. Y. 83;

*Rivers* v. *A. & C. Wright Co.*, 43 Southeastern 499;

*Muller* v. *Kling*, 209 N. Y. 239;

*Fourth St. National Bank* v. *Yardley*, 165 U. S. 634;

*Fortier* v. *Delgado & Co.*, 122 Fed. 604;

*Hackett* v. *Campbell*, 10 App. Div. (N. Y.) 523, aff'd 159 N. Y. 537.

The case of *Coates* v. *First National Bank of Emporia*, 91 N. Y. 20, is a leading authority. The facts were as follows:

The First National Bank of Emporia, Kansas, was a depositor in the Mastin Bank of Kansas City. Both the Mastin Bank and the First National Bank were depos-

itors in the bank of Donnell, Lawson & Co., in New York City. On July 30, 1878, the First National Bank of Emporia, having then more than $5,000 on deposit in the Mastin Bank, directed the Mastin Bank, by letter, to remit $5,000 to Donnell, Lawson & Co. "for our account; credit and charge our account." On August 1st, the Mastin Bank received this letter and acknowledged it, advising "We remit $5,000 to Donnell, Lawson & Co., New York, to your credit." The Emporia Bank, upon receipt of the letter, credited the Mastin Bank with $5,000 and charged that amount to Donnell, Lawson & Co. On August 1st, the Mastin Bank mailed to Donnell, Lawson & Co., a paper reading

> "Pay to the order of credit, the First National Bank, Emporia, Kansas five thousand dollars.
> To Donnell, Lawson & Co."

accompanied by a letter to Donnell, Lawson & Co. to the effect that they would find enclosed, for the credit of the Emporia Bank, $5,000. On mailing this letter the Mastin Bank charged $5,000 on its books to the Emporia Bank and credited that amount to Donnell, Lawson & Co.

Two days after these transactions the Mastin Bank assigned to the plaintiff.

Donnell, Lawson & Co. received notice of the assignment by telegraph from plaintiff August 5, 1878, and on the same day, a little later, the letters and orders above mentioned were received by them.

The plaintiff, as assignee of the Mastin Bank, demanded payment of the balance appearing to be due to the Mastin Bank at the date of the assignment. The defendants also demanded payment of the orders. Donnell, Lawson & Co. paid into court the full amount of the

apparent credit and thereupon the defendants were substituted in their place as defendants.

The object of the suit was to determine the title to this fund.

The Court said:

> "* * * It seems to be well settled that a mere check or draft does not operate as an assignment or appropriation of the drawer's deposit in favor of the payee before acceptance by the bank (*Harris* v. *Clark*, 3 N. Y. 93; *Atty. Genl.* v. *Continental Life Ins. Co.*, 71 id. 325; 27 Am. Rep. 55), but the doctrine has not been extended beyond instruments of that character, drawn in the ordinary form; nor to a transaction not restricted to the very terms of such paper. * * *
>
> "I am unable to see why, on the first day of August, there was not a complete and consummated contract between that bank and the Mastin Bank. The Mastin Bank, up to that day, owed the Emporia Bank, and was requested to pay its debt by transferring funds then with Donnell, Lawson & Co. They say by letter, 'we will do so,' at once charge the Emporia Bank, and credit themselves with $5,000; on the same day, by letter, they inform the Emporia Bank that this has been been done, and in fact they direct Donnell, Lawson & Co. to 'pay to the order of credit, the Emporia Bank,' the sum named. The Emporia Bank also credited the Mastin Bank with it. These circumstances in the conduct of both parties establish an agreement, the effect of which, as between the Mastin Bank and the Emporia Bank, was to estop the former from setting up that so much of the credit to which they were before entitled from Donnell, Lawson & Co. did not belong to the Emporia Bank, and the Emporia Bank from saying that so much of the debt before due from the Mastin Bank to it had not been extinguished. (*Allen* v. *Culver*, 3 Den. 284.

292). Written out, the contract indicated by the book entries and the correspondence is one of assignment of so much of the credit, or funds then to its credit with Donnell, Lawson & Co., to the Emporia Bank, and a discharge of a debt due by it to that bank. *The whole was completed the moment the letter of the Mastin Bank to the Emporia Bank was placed in the post-office.* • • •

"Nothing further remained to be done. • • • As between these parties the credit or funds had ceased to be the property of the Mastin Bank. The Emporia Bank was no longer creditor, because it was paid. The credit, or right to call upon Donnell, Lawson & Co. for the same amount, was the means of payment. • • •

"• • • Here by the act of the customer, the title to the account itself had passed from him, and the check, or order, as it may more properly be called, was, between the customer and the assignee —the Emporia Bank, of no importance. *The bankers, by virtue of the assignment, owed the money specified in the account, to the Emporia Bank, and it was not a matter as to which they had any discretion to exercise.* • • •"

The Court, after citing *Burns* v. *Carvalho*, 4 M. & C. 890, a leading English case, continued:

"In the case before us, as in that, there was an existing fund in the agent's hands and a distinct contract by the debtor with its creditor, to discharge the liability out of that fund, and to give directions for that purpose. • • •

"I have not overlooked the contention of the respondent that the entries were mere matter of bookkeeping for the convenience of the bank. It might be so if they stood alone. But taken in connection with the letters between the parties, and

the order and letter of advice sent to Donnell, Lawson & Co., *they are equivalent to an actual transfer of credit, or account; to an assignment, therefore, at least in equity, of the fund in the hands of Donnell, Lawson & Co.* * * *

"In *Pratt* v. *Foote* (9 N. Y. 463) the plaintiff, a private banker, was held charged as on an agreement by entries made in the books of his bank, although not communicated to the defendant, and the latter was relieved from an obligation by reason of them. *In the case before us the entries were preceded by the letter of the Emporia Bank, requesting a transfer of credit, accepted by the Mastin Bank, and the books made to conform thereto. Taken together they conclude the Mastin Bank and of course its voluntary assignee.* * * *

"It follows that the fund did not pass to the assignee. (*Hopkins* v. *Banks*, 7 Cow. 650; *Muir* v. *Schenck, supra; Osborn* v. *Thomas* 46 Barb. 514). The assignment to him is dated August 3; it purports to transfer the property 'and credits' of the Mastin Bank; of course it speaks as of the day of its date, *and on that day the credit in question was not its property. It could not withdraw or change its application and so revive its indebtedness to the Mastin Bank, or that of the defendants to itself.* It does not appear, however, that the Mastin Bank undertook to again deal with this fund, or to assign it to its trustee, nor, if it had been possible to do so, that it undertook to deprive the defendants of the benefit of the contract under which they claim. It follows from these observations that the learned referee erred in finding that the money in question passed by assignment to the plaintiff, and that the defendants were not its owners."

The other cases cited above are to the same effect.

The Trustee relies on *Re Interborough Corp., Noyes* v. *Bank* and *Eastman-Kodak* v. *Park Bank* as authorities against the claimant (Brief, pp. 21, 23, 24).

These cases are clearly distinguishable from the present case and the *Interborough* case expressly recognizes the distinctions and points out that the result would have been different if there were present some or all of the circumstances which are present in the case at bar. That case is really an authority in the claimant's favor. It involved the relation of debtor and creditor between the corporation and its bank and merely held that where a depositor, for its own convenience, directs that a portion of its funds shall be carried in an account against which checks for interest on bonds will be drawn, the bondholders acquire no trust in the deposit. *The court expressly recognized that if the creditor were told of the setting apart, and assented thereto, a different situation would arise* (288 Fed. p. 345), citing from *Story on Equity:*

> "* * * But if upon notice the creditors should assent thereto and no intermediate revocation should have been made by the assignor or remitter, there in equity the assignee or mandatary will be held a trustee for the creditors. * * *
>
> "* * * It may be revoked at any time before it is executed, or at least before any engagement is entered into by the mandatary with the third person to execute it for his benefit; and it will be revoked by any prior disposition of the property inconsistent with such execution. *But if no revocation is made and the mandate continues in full force, the trust as such continues for the benefit of such third person who after his assent thereto notified to the mandatary may avail himself of it in equity without any reference to the assent or dissent of the mandatary upon such*

> ***notice; for his receipt of the property binds him to follow the orders of his principal.***"

In our case it was well understood between the parties that the fund would be created abroad. In fact the claimant entrusted the Bankrupts with its money on the faith of the Bankrupts' assurance that that would be done, the Bankrupts, in their "Drawing Service" having agreed to

> "provide the drawee with funds sufficient for the payment of the draft abroad, by a transfer of credit from our balance, or otherwise."

Hence the foregoing quotation from the *Interborough* case applies. In the *Interborough* case the court pointed out that the money on deposit in the bank (p. 346)

> "was not received by the latter under instructions to distribute it among specified creditors, or to the coupon holders. It was received by the Empire Trust to be paid out on account checks to be drawn by the Interborough and directed to be charged against the separate account which had been created."

In our case there was no such situation. The money set apart by the Banca Commerciale Italiana was to be paid against the draft drawn by claimant and not upon any subsequent order of the Bankrupts.

The following principles were laid down as established by the court in the *Interborough* case (p. 347):

> "If A. places money in the hands of B., to be delivered to C., a trust arises in favor of the latter. The acceptance of the money with notice of its ultimate destination creates a duty on the part of B. to devote it to the purpose intended, and a court of equity will enforce the trust. *McKee* v. *Lamon*,

159 U. S. 317, 322, 16 Sup. Ct. 11, 40 L. Ed. 165. In this instance also A. parted with control over the fund when he placed it in B.'s possession.

"Every person who receives money to be paid to another, or to be applied to a particular purpose, to which he does not apply it, is a trustee, and may be sued either at law for money had and received, or in equity as a trustee, for a breach of trust."

thus recognizing the very rule for which we contend. The rule for determining whether an equitable assignment exists, as stated in 19 American and English Encyclopedia of Law, Second Edition, page 16, was adopted by the court in the following language (p. 349):

"But a mere agreement to pay a debt out of a designated fund does not give an equitable lien upon the fund, or operate as an equitable assignment thereof. *There must be an appropriation of the fund protanto, either by giving an order, or by transferring it otherwise in such a manner that the holder is authorized to pay the amount directly to the creditor without the further intervention of the debtor.*"

In our case there was an appropriation of the fund, both by the giving of the order from the Bankrupts to Banca Commerciale Italiana and by the transferring of the money by Banca Commerciale Italiana from the Bankrupts' account to Banca Commerciale Italiana's unpaid draft account, out of which the Banca Commerciale Italiana was

"authorized to pay the amount directly to the creditor without the further intervention of the debtor."

The court also recognized the rule (p. 349):

> "• • • But it is now definitely settled in the Federal Courts that a promise based on a consideration to pay out of a particular fund creates a lien on the fund, which attaches to the fund when it comes into existence and which equity will enforce, holding the promisor to be a trustee as soon as he gets title. *Barnes* v. *Alexander*, 232 U. S. 117, 120, 121, 34 Sup. Ct. 276, 58 L. Ed. 530."

It is perfectly apparent from what has been said, that the *Interborough Consolidated Corp.* case is not only no authority against the claim of the claimant in this proceeding, but that in that case the court distinctly recognized that if there were present there some of the facts and circumstances which are present here, an equitable assignment would have resulted.

The *Noyes* case was almost identical on its facts with the *Interborough* case. For the same reasons stated with respect to the *Interborough* case, the *Noyes* case is not an authority against the claimant. It held merely that where a corporation deposits its money in a special account *in its own name*, to meet interest coupons on bonds as they become due, there is created merely the relation of debtor and creditor and the depository does not become a trustee in favor of the coupon holders. In that case the corporation opened a bank account designated by the bank "Chicago, Rock Island & Pacific Railroad Co., Coupon Account," and transferred to this account a sum of money from the corporation's general account. The money still was in an account in the depositor's name. In our case the money was taken out of K., N. & K.'s account and put into the foreign bank's own account, which it called "Drafts Payable," and which was

a record of "its" obligations on drafts advised. This account, as Dawson testified, was the record of moneys set aside "in a special fund awaiting the presentation of any drafts against that fund." It was a fund which performed the same function as was originally accomplished by the drawee banker by putting "the money in his box or in his office" there to be held "useless, awaiting the presentation of the commitment or draft." Surely there is no analogy between such a fund and money which a depositor puts into his bank under circumstances like those in the *Interborough* and the *Noyes* cases. The distinction is, that although a fund may be designated as the fund out of which certain commitments will be paid, that fund does not become the property of the holder of the commitment *as long as the fund remains in the depositor's name and under his dominion*. As we have shown, the money in the "Drafts Payable" account was not the property of K., N. & K.

In the *Eastman* case, the depositor merely directed his banker to pay checks drawn by the depositor. This direction, though given with respect to specific checks, added nothing to the obligations of the banker, because it was the banker's duty, irrespective of this notification, to pay the checks drawn by the depositor as long as the depositor's account contained sufficient moneys. In that case the banker did not, upon receipt of the notice, charge the depositor's account and credit the funds to another account in which the bank kept a record of *its* commitments; there was no notification by the bank that it had so debited the depositor's account and credited its own account; there was no approval of this procedure by the depositor, as there was by K., N. & K. in the case at bar. The money always remained the deposi-

tor's money in an account in the depositor's name. The *Eastman* case bears no resemblance to this case and is no authority against the claimant here.

It is unnecessary to discuss the other cases cited by the Trustees in Point I of his brief because they are in the main subject to the same comments as the *Eastman* and the *Interborough* and the *Noyes* cases.

The authorities establish that there was an assignment by the Bankrupts of their funds in the hands of the Italian Bank for the payment of the draft and that the money so assigned ceased to be the property of the bankrupts; that once the assignment took place, the bankrupts had no right to countermand or interfere with it. The Receiver can have no greater rights than the Bankrupts; hence the money does not belong to him. It is stipulated (fols. 330-331):

> "That after the draft in question was presented and payment refused by the Banca Commerciale Italiana, the draft was returned to the purchaser, Bachisio Tabasco, and that thereupon the First National Bank of Trinidad paid to the said Tabasco the sum of $1,128.87 and thereupon the said Tabasco delivered the said draft to the First National Bank of Trinidad."

The assignment of the funds in the hands of Banca Commerciale Italiana was made to "protect" the said draft and Banca Commerciale Italiana thereupon held the money "as a special fund" and "for a particular purpose," to wit: "Awaiting the presentment of the draft" (fols. 348, 356-357).

The draft was duly presented and by the Receiver's direction not paid. The money was remitted to the Receiver who, in turn, turned it over to the Trustee. The

Claimant, which issued the draft and provided the Bankrupts with the money with which to protect it, are now the owners of the draft. In these circumstances the money belongs to it.

> *Cutler* v. *Bank*, 113 N. Y. 593;
> *Kingman* v. *Hotaling*, 25 Wend. 423;
> 8 *Copus Juris*, pages 83-372-831-1004;
> and cases cited *supra*.

The Trustee contends (p. 5) that there was no equitable assignment because there was no obligation on the part of K., N. & K. to create the fund "in advance," its obligation being merely to have funds in the foreign bank applicable to the payment of the draft when the draft is presented. While it would not make any particular difference in the circumstances of this case whether there was or was not such an obligation, owing to the fact that the credit was actually *created* and maintained until long after bankruptcy, it should be observed that the Trustee's statement of the Bankrupt's obligation does violence to the precise terms of the drawing service, which provide *not* that the Bankrupts should cause the necessary balance to be in the hands of B. C. I., by the time the draft should be presented, but that upon the receipt of the advice of the drawing of the draft

> "our advices are *at once* forwarded and funds provided with the respective drawee banks for the payment thereof" (fol. 420),

and which also provide (fol. 422) that upon receipt of the advice

> "we shall *promptly* forward our advice of the same and provide the drawee banks with funds sufficient for the payment of the draft abroad."

Whatever may have been the practice of the Bankrupts with respect to delaying their notifications to the foreign banks,—that is, speculating against the market without the knowledge of the inland banks—the fact remains that under the drawing service *they represented to the inland banks that they would provide the fund abroad "promptly" and "at once" upon the receipt by them of notice that the drafts had been drawn* and "adequate funds" to cover payment. They did *not* merely undertake that by the time the draft would be presented they would have a sufficient *credit* there. Their credit was not involved. The drafts were neither *drawn* by them nor *payable* by them and the holder of the draft would have no claim against them nor recourse to any balance in their favor.

The Trustee argues (p. 32) that the absence of an equitable assignment is to be inferred from the circumstance that K., N. & K. did not direct the foreign bank to set up an account in favor of claimant, but that the foreign bank credited all drafts advised

"in an omnibus Draft Payable account."

The foreign bank could, of course, if it had chosen, have credited the moneys to an account in claimant's name, but that was not the *only* method and the failure to adopt that method does not indicate that some other method was just as effective. K., N. & K. had no control over the foreign bank's internal bookkeeping procedure and was not interested in the manner in which the foreign bank made a record of its obligations. From the

point of view of the foreign bank, however, the bookkeeping involved in carrying their obligations on drafts advised in the "Accounts Payable" account, was much simpler than setting up a separate account in favor of each of the thousands of inland banks which might draw drafts under the Drawing Service and that is probably why this method was adopted.

The evidence shows that upon receipt of advice of the drawing of a draft, B. C. I. credited the necessary amount to the "Draft Payable" account *and made appropriate notations to show that the sum so credited was to be applied to the payment of the particular draft* (see fol. 508 *et seq.*) In crediting moneys to meet drafts advised to "Drafts Payable" account B. C. I. created an account which, in legal effect, was exactly the same as the special account usually maintained by a lawyer, in which he deposits collections made on behalf of his clients. He does not open a separate trust account for each client each time he makes a collection. He has one omnibus account in which he deposits all such collections. It is a trust account for the benefit of his clients to the extent that their funds respectively have been put into it. So it was with the "Drafts Payable" account of B. C. I. The moneys which went into it they held for particular purposes, to wit: the payment of the various drafts noted in it. There was a trust in favor of the holder of each draft to the extent that money for the payment of that draft was in the account and the mere fact that this method was adopted in preference to opening separate accounts in favor of the respective drawer banks is of no greater significance than the lawyer's failure to open a separate trust account for each client for whom he makes a collection.

The entering of a notation of the name of the bank whose account had been charged with the moneys credited to the "Drafts Payable" account by no means indicated, as the Trustee asserts (pp. 33-34), that the moneys credited to the "Drafts Payable" account "still belonged to K., N. & K." Mr. Dawson, in whose testimony this statement is claimed to find support, gave no such evidence. What he said was (fol. 350) that when the credit was made in the "Unpresented Drafts Drawn" account (meaning the "Drafts Payable" account), an entry was also made of the bank "whose account has been charged." This is an entirely different statement from what the Trustee's Brief attributes to Dawson. The entry referred to by Dawson is simply the common, everyday "cross entry," by which an item in an account can be traced back to the source from which it came. The entry merely facilitated B. C. I. in determining from the account of which of its depositors the particular item credited had come.

The Trustee urges that there could not have been an equitable assignment because the holder of the draft did not know of the provisions of the Drawing Service or of the creation or the existence of the "Drafts Payable" account (p. 9). It was entirely unnecessary for the holder of the draft to know any of these facts. An equitable assignment would result, not from the facts known to the holder of the draft, *but from the acts and conduct of the Bankrupts and their foreign correspondents.*

## POINT II.

**Moneys remitted to the Bankrupts in connection with the drawing of a draft under the terms and provisions of the Bankrupts' Drawing Service were received by the Bankrupts as agents of the remitter for the purpose of applying the same to the payment of the draft.**

Not only is the agreement clear upon the relationship of the principal and agent, *but the very nature of the transaction shows that an agency was intended.* The Claimant had drawn a draft payable in Italy. It was necessary *for the Claimant* to provide the foreign bank with money with which to pay the draft when presented. This the Claimant could do in one of two ways. It could either *personally* provide the drawee bank with the money for use in paying the draft when presented, or else it could engage *someone else* to do so for it. The Bankrupts held themselves out as peculiarly well fitted to act as Claimant's "agent" for the performance of this "function." They stated that if the necessary funds were sent to them, they would notify the drawee bank of the drawing of the draft and "provide for the payment thereof," pointing out on two separate occasions and in the clearest terms that in the performance of this "function *we act as agents of the drawers.*" There can be no doubt about the nature and the subject of the agency. The Bankrupts undertook, as the Claimant's agent, to perform *for the Claimant* a "function" which the Claimant would otherwise have had to

perform itself, to wit: *put into the hands of Banca Commerciale Italiana the money which the Claimant would provide for the purpose of meeting the draft which the Claimant had drawn.* In addition to describing themselves as "agents," the Bankrupts estopped the inland banks from claiming that K., N. & K. were something more than agents by providing in the "Issuing Banks Record" (fols. 479-480), (being the stub in the book of Foreign Drafts, which would remain with the issuing bank after the draft was issued and the advice mailed to K., N. & K.) that the moneys paid to K., N. & K. were paid to them as "*Transfer Agents.*"

The relation of principal and agent is expressly provided for in the Drawing Service, which constitutes the written agreement between the parties; this agreement was prepared by the Bankrupts in language chosen by them; even if the undertaking to act as agent were not as clear and as unequivocal as it is, the language would have to be construed against the Bankrupts, who selected it. The inland banks, in drawing drafts and in entrusting their money to the Bankrupts under the provisions of the Drawing Service, had a right to, and did, rely upon the existence of this relationship. The nature of the transaction shows that the word "agent" in the Drawing Service was intended to mean what it said. In these circumstances the appellant respectfully urges that the position of the Claimant should not be prejudiced upon the theory that the words of the Drawing Service did *not* mean what they said.

A reference to the legal precedents shows that the principles involved are neither new nor novel but on the contrary have been frequently stated and authoritatively decided.

The rule has long been established in England that sums of money delivered to a bank for the payment of an obligation of the payor at some other place is money held by the bank in trust for a specific purpose and if not so applied belongs to the payor. The leading English case is *Farley* v. *Turner*, 26 L. J. Ch., 710. It has been frequently cited and followed in the American decisions. In this case one Goodwin having accepted a bill, payable at Robarts & Co., paid into the hands of his bankers, Messrs. Farley, Turner & Jones, the sum of £707. He told the bankers' clerk that £500 of this money was to be used to meet said acceptance on December 14th, and he notified Farley, Turner & Jones in writing to advise Robarts to pay the same. The bankers thereupon sent to Overend & Gurney certain bills to discount and directed them to pay the proceeds to Robarts for the purpose of meeting Goodwin's acceptance, as well as others. This was done on the 11th of December and on the morning of the 12th Robarts received information that Mr. Turner of the firm of Farley, Turner & Jones, had died the preceding evening and the firm had ceased to carry on business. The £500 was not applied in payment of Mr. Goodwin's acceptance but was subsequently paid over to the representative of Mr. Turner's estate. Vice-Chancellor KINDERSLEY held

> "that the £500 belongs specifically to Goodwin and not to the general creditors of Mr. Turner."

In the course of his opinion he said (p. 711):

> "According to the statement in the case, it appears that at the time of paying in the £707 Goodwin told the clerk that £500 of this money was to be applied for the specific purpose of meeting an acceptance payable at Robarts & Co.'s, to become due on the 14th. Goodwin at the same

time signed the notice before stated. Now, what was the effect of this direction to the bankers? Goodwin in effect said, 'There is a bill which I want paid at Robarts & Co, therefore send them £500 of this money and advise them to apply it in payment of this bill.' The direction is accepted by the bankers, or by their clerk, which amounts to the same thing, and the clerk did what appears to be usual. There was no negligence on his part; at the same time he placed the whole amount of £707 to Mr. Goodwin's general banking account. He might certainly have sent up a cheque for £500 to Messrs. Robarts & Co., and placed the remaining sum to Mr. Goodwin's account, but he took the ordinary course and sent up the £500, debiting Mr. Goodwin's banking account with that sum, and they informed Robarts & Co. that such a bill would be presented. Now, it so happened that the Kidderminster Bank had other bills, more or less under similar circumstances, which they wanted paid at Robarts' bank, and they sent up a batch of bills to Messrs. Overend & Gurney for them to discount, and directed them to pay the amount into Robarts & Co.'s bank for the purpose of meeting other bills, as well as that for £500. It appears to me that the course pursued was the same as if, having no occasion to pay more than the £500 bill, they had simply sent up the specified amount with a direction to pay that particular bill. *It is true that the money was not earmarked as if it had been locked up in a box, but it is a portion of the £707 which had been paid in expressly for the purpose of meeting the bill for £500.* The facts of this case differ, I think, from the cases cited. I admit that the money is not a particular deposit with the bankers, but *it is money placed in their hands to be applied in a particular way.* What I now decide will not trench upon the authorities which decide that money paid into a banker's is not a deposit

which you may receive back in the identical notes and sovereigns, but that it is a debt. *That is quite a different case.*"

See also, *Giles* v. *Perkins*, 9 East. 12, and *Burdett* v. *Willett*, 2 Vernon 638.

The American rule, both State and Federal, follows closely the law of England and is stated in the following cases:

*In re Jarmulowsky*, 258 Fed Rep. 231;
*In re A. Bolognesi & Co.*, 254 Fed. Rep. 770;
*City of St. Louis* v. *Johnson*, 5 Dillon 241;
*Massey* v. *Fisher*, 62 Fed. Rep. 958;
*Moreland* v. *Brown*, 86 Fed. Rep. 257;
*People* v. *City Bank of Rochester*, 96 N. Y. 32;
*Cutler* v. *American Exchange Natl. Bank*, 113 N. Y. 593;
*People ex rel. Zotti* v. *Flynn*, 135 App. Div. 276;
*Peak* v. *Ellicott*, 30 Kansas, 156, 1 Pac. 499;
*Ryan* v. *Phillips*, 3 Kans. App. 704, 44 Pac. Rep. 909;
*Star Cutter Co.* v. *Smith*, 37 Ill. App. 212;
*Roca* v. *Byrne*, 145 N. Y. 182.

In *City of St. Louis* v. *Johnson* (5 Dillon 241) the plaintiff kept two accounts in the National Bank of the State of Missouri (which suspended payment and went into liquidation on June 19th, 1887). From these accounts the City drew moneys from time to time to provide funds for bonds and coupons of the City falling due and payable in the City of New York. It was the custom

of the City Treasurer to draw a check on the National Bank of the State of Missouri for the amount necessary to be placed in the New York bank to pay maturing bonds and coupons, endorse the check and deliver it to the bank with written instructions to remit the amount to the National Bank of the Republic or the National Bank of Commerce in the City of New York to pay bonds and coupons of the City of St. Louis falling due. Thereupon the National Bank of the State of Missouri would remit or provide a credit for the amount specified to the New York Bank with written instructions to the said Bank to pay and charge to the general account of the National Bank of the State of Missouri the bonds and coupons of the City of St. Louis maturing at said Bank and to forward the same cancelled to the National Bank of the State of Missouri. The National Bank of the State of Missouri paid the City of St. Louis interest on its average daily balance in its current account but none on the sums remitted to New York after the bank received the check of the City Treasurer therefor. The Court said:

> ... The bank was the general debtor of the city, having funds subject to its check or draft. Let us take the transaction of April 25th, for it represents all the others. The city comptroller directs the city treasurer 'to remit' to the Bank of the Republic $51,000 to pay the bonds and coupons of the city falling due at that bank on the following month. On the same day the city treasurer draws in favor of the bank his check for the amount and encloses it to the president of the bank, with directions, *inter alia*, 'to remit' to the Bank of the Republic, in New York, $51,000, 'to pay bonds and coupons of the city falling due (at that bank) in May next.' The bank at once charges the amount of that check to the city, which

has the effect to reduce the city's balance with the bank and to stop interest to that extent. If the money had been passed over the counter to the city treasurer, and he had delivered it to another bank, with instructions to remit to a particular bank for a specified and definite purpose, such bank would have been the agent of the city to remit or transmit the money of the city; it would remain the money of the city, notwithstanding it may have been credited on account to the agent, and not to the principal, and this with the consent of the two. If such bank had transmitted the money by express, the money would be the city's; if by draft, it would be the agent of the city for that purpose; but when its instructions were obeyed and the money duly received by the appointed depository, all liability would be at an end. If the appointed depository failed, the loss could not be thrown upon the agent.

"But the money was not paid over the counter ot the city, and the city did not select some other agent or bank to remit or transmit it to the Bank of the Republic, but selected its general depository to make the remittance, and accepted a credit in another account for the same sum. The bank remitted the sum, as directed by the city, to the Bank of the Republic, with specific directions to credit the amount to it, and to use the same 'to pay the bonds and coupons of the city maturing at your bank next month,' and charge the amount to the account of the bank here, and forward to this bank the bonds and coupons cancelled.

"The letter of the treasurer to the president of the bank made the bank here the agent of the city to remit, and if the bank here did remit accordingly, and placed the sum with the designated bank, i. e., the Bank of the Republic, it did its duty, and would not be liable to the city if the Bank of the Republic had failed with this fund on hand. * * *

"The bank charged the city with exchange on the amount it thus received, the same as it would have charged if the draft had been for any other customer. It became the agent of the city to transmit the money. The money, when placed in the Bank of the Republic, was, as between the Missouri bank and the city, the money of the latter. When the agent presented coupons cancelled, this showed that the agent had discharged the duty it had undertaken.

"It is my judgment that the relation between the Missouri bank and the city, as respects the money deposited with the Bank of the Republic, was not that of debtor and creditor strictly, but that of principal and agent, with the duties and liabilities of the latter, and not those of the former relation. The moneys deposited by the Missouri bank in its name with the Bank of the Republic, were, as between the former bank and the city, *trust moneys*, and in equity they belong to the *cestui que trust*, and the latter has the right to pursue and claim them as against all persons who do not stand free of the trust."

The other cases cited above are to the same effect.

The Trustee relies on *Legniti* v. *Mechanics & Metals Natl. Bank*, 230 N. Y. 415, and *Beecher* v. *Cosmopolitan Trust Co.*, 239 Mass. 48, in support of his claim that there was initially no trust relationship.

In the *Beecher* case the plaintiff, as appears from the opinion (page 52) paid money to the trust company in consideration

"of an agreement by the defendant trust company that it would procure and provide funds in Roumania to meet *the order which it had sold and delivered to the plaintiff*."

The case involved merely the purchase and sale of credit. The plaintiff had bought from the defendant a remittance order, which is similar to a draft, and the case is an authority only in cases of purchases and sales of credit (See *Equitable* v. *Keene*, 232 N. Y. 290, 295).

The Trustee relies on the *Beecher* case because in the printed receipt given to the purchaser appeared the words: "It is expressly agreed that Cosmopolitan Trust Company acts as agent only for the sender." It will be observed that these words were not contained in any *contract*. They were contained merely in a "receipt" which was probably a printed form, broad enough in its terms to cover every transaction which might arise, including those in which an agency might exist. The words quoted could not have been intended to apply to the transaction with the plaintiff, because the transaction was a *sale;* there was no "sender" for whom the Trust Company could act as "agent" and no possibility of an agency in the circumstances of the case. In the present case, on the contrary, the provisions for an agency are expressed in a long and carefully drawn *contract*, which is clear and explicit, which is applicable to transactions of the nature of the one here involved *and was drawn expressly for use in such transactions*. The *contract* here is not in the same category with the *receipt* issued in the *Beecher* case, nor are the facts and circumstances of this case similar to those of the *Beecher* case. In the *Beecher* case the bank sold its credit. It drew its *own* draft payable abroad, and in consideration therefor the plaintiff paid his money. In the case at Bar the Bankrupts did *not* draw their own draft (folios 419, 474). In conformity with the Drawing Service the draft was drawn by the claimant in its own name, "for its own account as principal and our

(K., N. & K.'s) name does not appear" (folios 419, 474). The holder of the draft acquired no right against K., N. & K. They had, for a consideration, merely agreed to receive a fund provided by the maker of the draft "to cover" its payment and to accept "*employment*" from the maker (folio 423) as its "*Agent*" to provide the drawee bank "at once" with the money for the payment thereof. The use of these protective clauses was not accidental or inadvertent. They had a very definite purpose in limiting their relation to that of an agent; they were guarding against any responsibility for defaults by the foreign banks after the fund was delivered to them. They were not unfair or unreasonable in taking this precaution because their profit did not justify their assuming any such obligation. We respectfully submit that this is altogether a different case from the sale of credit involved in the *Beecher* case. As the court said, the undertaking of the bank there "was a contract obligation, based upon the payment of the money, to have funds in Bucharest with the bank, which funds should be sufficient to insure the payment of the order on presentation." There was no such obligation on the Bankrupts here. It was immaterial whether they would have credit with the B. C. I. at the time the draft would be presented. Their obligation was merely to see that the fund with which to pay the draft was delivered to B. C. I., and this obligation they assumed only upon the prior receipt by them of the equivalent amount, plus their charge for the service. They did not even need to have an account with B. C. I. They could provide the fund "by transfer of credit from our balance, *or otherwise*" which means as the Court pointed out in the *Legniti* case "in any form recognized in financial circles." The outstanding point

about the *Beecher* case and the other cases cited by the Trustee is that in all of them the banker drew against its own credit abroad and *merely undertook that it would have a credit balance in the foreign depository at the time its order was presented there.* Hence the transaction is described as a purchase and sale of credit. In such cases

> "the seller engages that he has the balance at the point on which the payment is ordered" (*Legniti* v. *Bank*, 230 N. Y., at p. 420).

In the present case there is no such situation. There was no representation by K., N. & K. that they had such a credit balance or that they would have such a credit balance on the date of the presentation of the draft and neither Claimant nor the holder of the draft was concerned with that question. The draft was not drawn by K., N. & K. and no recourse could be had against its balance for the payments thereof.

The *Legniti* case cited by the Trustee (page 43) was also a sale of credit. In that case the plaintiff purchased a cable transfer. In such cases, as the court pointed out (page 420) there is involved

> "a method of transmitting money by cable *wherein the seller engages that he has the balance at the point on which the payment is ordered* and that on receipt of the cable directing the transfer his correspondent at such point will make payment to the beneficiary described in the cable. All these transactions are matters of purchase and sale and create no trust relationships."

There was in our case no engagement by the Bankrupts that they had "the balance at the point on which the payment is ordered" and there was no requirement

that they should have it. In our case they merely undertook, as the claimant's agents, upon being first supplied with the necessary moneys, to provide the fund abroad with which to pay the draft drawn by the claimant. The court distinctly recognized the distinction between cases calling for the transmission of money abroad and those in which only a credit is purchased (pp. 420-421) and said that in the former cases

> "the bank or transmitter is the agent of the person paying the money, and until the money is sent holds it as agent or trustee for the owner. Such were the cases of Musco v. United Surety Company (132 App. Div. 300) and People ex rel. Zotti v. Flynn (135 App. Div. 276). In these latter transactions the intention of the payer is that the money he gives to his agent shall be sent abroad. It is the amount which he gives that is to be transmitted. *How it is sent may be immaterial to him. If there be time, currency might be purchased and sent. If not, it may be transmitted in any form recognized in financial circles. It is not at all necessary that the sender or agent have credit in the place to which the money is to be sent.*"

These words apply to our case. A certain amount was to be transmitted. How it was sent was immaterial to us. It could be "transmitted in any form recognized in financial circles" and it made no difference whether K., N. & K. had an account there or not.

The Trustee asks (pp. 40-41):

> "Does the respondent seriously argue that the intention underlying the drawing service as agreed to by the parties was that the large and small banks scattered throughout this country who had no knowledge of foreign banks and bankers, were

paying over their money to K., N. & K., relying on the credit, solvency and responsibility of foreign correspondents in scattered communities throughout Europe, wholly unknown to them and chosen by K., N. & K.?"

We have no hesitation in saying that in our opinion, under the terms of the Drawing Service, K., N. & K.'s obligation ceased the moment they put into the hands of the foreign bank a fund "sufficient to cover" payment of the draft and that they were in no respect responsible for the acts, omissions, derelictions or defaults of the foreign bank thereafter.

K., N. & K. submitted a list of foreign correspondents. It made no representations as to their financial responsibility; that was a matter the inland banks could investigate before using any of them if they chose. K., N. & K. agreed merely, as the *employee* and the *agent* of the inland bank, to provide the foreign bank with a fund equivalent to the one supplied to them by the inland bank. K., N. & K. represented that they had better facilities for doing this than the inland bank itself had—*and that is the only reason the inland bank used K., N. & K. rather than send the currency direct.* The limit of K., N. & K.'s obligation was to provide the fund to the bank abroad—thereupon their responsibility ceased. They were not responsible for any acts or omissions of the foreign bank after that. It must be clear to the Court that any other interpretation of K., N. & K.'s obligation would make K., N. & K. the guarantor of the financial responsibility of every one of the hundreds of scattered correspondents named in the list, as well as of their performance

of their agreement to meet the draft when presented. Considering the small fee which was paid for the service, it must be obvious that the inland bank did not expect and K., N. & K. never intended to assume such an obligation. Once the money was put into the hands of the foreign bank, K., N. & K. was "through"—so thoroughly through *that the foreign Bank never even advised what drafts had been paid and K., N. & K. were not interested to know* (fols. 160, 161, 433). The magnanimous offer by the Trustee to treat K., N. & K.'s obligations as one which continued until payment was accomplished cannot be considered seriously in view of the fact that K., N. & K. is in bankruptcy. The Court will not be slow to recognize that if K., N. & K. were *solvent* and the *foreign* bank had failed, K., N. & K. would be loud in their protestations against any such construction, and would forcefully and rightfully point to the terms of the Drawing Service, which shows that K., N. & K. were but *employees* and *agents* for a particular purpose; that the claimant's money had been sent to them as "Transfer Agents"; that they have performed the service for which they were employed, by putting into the hands of the foreign bank the fund which the inland bank gave them for that purpose and that thereupon they were discharged. Loudest of all would probably be the claim that it would be unreasonable to suggest that for the insignificant fee paid K., N. & K. for their services the inland bank expected or that K., N. & K. undertook to become guarantors of the financial responsibility of every one of the hundreds of scattered correspondents named in the list and of performance by these correspondents.

## POINT III.

**The petition for a writ of certiorari should be denied.**

Respectfully submitted,

WILLIAM DEFOREST MANICE,
*Counsel for Respondent.*

WILLIAM DEFOREST MANICE,
ALLEN R. MEMHARD,
GEORGE TROSK,
*of Counsel.*

No. 130

Office Supreme Court
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DEC 5 19
CHARLES ELMORE

# Supreme Court of the United States

**October Term, 1927**

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THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy of Knauth, Nachod & Kuhne,
*Petitioner,*

*against*

THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO,
*Respondent.*

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## BRIEF FOR RESPONDENT

---

WILLIAM DEFOREST MANICE,
[redacted]
ATTORNEY FOR CLAIMANT - RESPONDENT

WILLIAM DEFOREST MANICE,
ALLEN R. MEMHARD,
GEORGE TROSK,
*of Counsel.*

# SUBJECT INDEX


| | PAGE |
|---|---|
| Statement of questions involved | 1 |
| The determinations of the Courts below | 2 |
| Facts relating to the question: Was there an equitable assignment | 2 |
| A. The provisions of the Drawing Service | 2–4 |
| B. The acts performed | 4–14 |


## Brief of the Argument


| | | |
|---|---|---|
| Point I | —Pursuant to the terms of the Drawing Service, K. N. & K. caused Banca Commerciale Italiana to create, out of K. N. & K.'s funds on deposit with Banca Commerciale Italiana, a fund for the payment of the draft involved in this proceeding. Thereby an equitable assignment was effected | 15 |
| | A. Equitable assignment depends on intention | 15 |
| | B. Terms of Drawing Service, as dicating intention | 15–18 |
| | C. Acts performed, as showing intention | 18–19 |
| | D. Legal precedents | 19–29 |
| | E. Discussion of Petitioner's contentions | 29–34 |
| | F. Discussion of authorities cited by Petitioner | 34–45 |
| | G. The claim of the Amicus Curiae | 45–46 |

PAGE

H. The speciousness of Petitioner's contention, as appears from its hypothesis that K. N. & K., for the trifling consideration received by it, agreed to become guarantors of the continued financial responsibility of everyone of the hundreds of its scattered correspondents throughout the world, as well as of their performance of their agreement to meet the draft when presented, and to remain such guarantors throughout the protracted period between the issuance of the draft and its presentation 46–49

I—Conclusion with respect to cause of action based on equitable assignment 49–52

Point II—The moneys remitted by Claimant to K. N. & K. were received by them in trust, as agents of the Claimant, for a particular purpose 52

A. Distinction between "Sale of Credit" cases and "Transmission Cases" 52

B. The terms of the Drawing Service 53–54

C. Answering Petitioner's contention that there was no agency 54–76

D. The legal precedents 76–95

E. Discussion of authorities cited by Petitioner 96–110

PAGE

Point III—Funds delivered to one in trust may be recovered by reclamation where the Trustee goes into bankruptcy without applying the property to the use for which he received it, providing the same can be traced ..... 111

Point IV—It is conceded that K. N. & K. did in fact create the fund which they agreed, under the terms of the drawing service, to create. The fund abroad was but a transmuted state of the money remitted by Claimant to K. N. & K. It was subject to the same equities. Upon the return of the money to the Receiver, at his request, and with knowledge of the Claimant's equities, the money stood in the place of the original remittance and the Receiver held it upon the same trust as Knauth, Nachod & Kuhne had held the original remittance ..... 112

A. Facts ..... 112–113

B. Legal precedents ..... 113–119

Point V—The Claimant agrees with the Petitioner that the rights of the parties became fixed upon the filing of the petition in bankruptcy and that the subsequent acts of the Receiver cannot change these rights ..... 119–121

Point VI—The decree of the Circuit Court of Appeals should be affirmed ..... 121

## Table of Cases


| | PAGE |
|---|---|
| American Sugar Refining Co. v. Fancher, 145 N. Y. 552 | 114, 115 |
| Beecher v. Cosmopolitan Trust Company, 239 Mass. 48 | 42, 96 |
| Bolognesi & Co., In re, 254 Fed. Rep. 770 | 78, 80 |
| Burdett v. Willett, 2 Vernon 638 | 78 |
| City of St. Louis v. Johnson, 5 Dillon 241 | 78, 81 |
| Coates v. First National Bank of Emporia, 91 N. Y. 20 | 19, 20 |
| Cutler v. American Exchange Nat'l Bank, 113 N. Y. 593 | 78, 85 |
| Duel v. Hollins, 241 U. S. 523 | 114 |
| Equitable v. Keene, 232 N. Y. 290 | 96 |
| Equitable Trust Co. of New York v. Rochling, New York Law Journal, Nov. 29, 1927 | 43, 61 |
| Erb v. Banco di Napoli, 243 N. Y. 45 | 40 |
| Farley v. Turner, 26 L. J. Ch. 710 | 76 |
| Fortier v. Delgado & Co., 122 Fed. 604 | 20 |
| Fourth St. National Bank v. Yardley, 165 U. S. 634 | 20, 27 |
| Giles v. Perkins, 9 East. 12 | 78 |
| Gorman v. Littlefield, 229 U. S. 19 | 114 |
| Hinkle Iron Co. v. Korn, 229 N. Y. 179 | 28 |
| Hutchinson v. LæRoy, 113 Fed. 202 | 113, 114 |
| Interborough Consolidated Corp., In re, 228 Fed. 334 | 34 |
| Jackson v. Tallmadge, 216 App. Div. 100 | 29 |
| Jarmulowsky, In re, 258 Fed. Rep. 231 | 78, 79 |
| Kuehne v. Union Trust Co., 133 Mich. 602 | 105 |
| Lægniti v. Mechanics & Metals Nat'l Bk., 230 N. Y. 415 | 32, 55, 58, 59, 65, 98, 99, 106 |

PAGE

Massey v. Fisher, 62 Fed. Rep. 958 ..... 78, 88
Matter of Pacat Finance Corporation, 295 Fed. 394 ..... 59, 106
Matter of Zimmerman & Forshay, 14 Fed. (2) 527 ..... 44
May v. LeClair, 11 Wall. 217 ..... 113, 114
Mooreland v. Brown, 86 Fed. Rep. 257 ..... 78
Muller v. Kling, 209 N. Y. 239 ..... 20, 24, 28
Muntean, Ex Parte, 13 Fed. (2) 730 ..... 44, 45

National Bank v. Ins. Co., 104 U. S. 54 ..... 111
National City Bank v. Hotchkiss, 231 U. S. 50 ..... 105
Noyes v. First Nat'l Bank, 180 App. Div. 162 ..... 34

Peak v. Ellicott, 30 Kansas 156 ..... 79
People v. City Bank of Rochester, 96 N. Y. 32 ..... 78, 84
People ex rel. Zotti v. Flynn, 135 App. Div. 276 ..... 79

Risley v. Phoenix Bank, 83 N. Y. 318 ..... 19
Rivers v. A. & C. Wright Co., 43 Southeastern, 499 ..... 20
Roca v. Byrne, 145 N. Y. 182 ..... 79
Ryan v. Phillipps, 3 Kans. App. 704 ..... 79

Samuels v. E. F. Drew & Co., 296 Fed. 882 ..... 104
Schmidt, In re, 298 Fed. 314 ..... 111
Star Cutter Co. v. Smith, 37 Ill. App. 212 ..... 79
Surety Co. v. Carroll, 194 Fed. 593 ..... 111

Taussig v. Carnegie Trust Co., 156 App. Div. 519 ..... 105
Throop Grain Cleaner Co. v. Smith, 110 N. Y. 83 ..... 20

Welch v. Polley, 177 N. Y. 117 ..... 114, 118

## Other Authorities Cited

American and English Encyclopedia of Law (2nd Ed.), Vol. 19, page 16 ..... 37
Bankruptcy Law, Section 70 ..... 120
Columbia Law Review, Vol. 21, page 510 ..... 89, 100
Corpus Juris, Vol. 2, page 423 ..... 71
Journal of the American Bankers Association, Vol. 16, No. 2 ..... 91
Perry on Trusts (6th Ed.), Sec. 828 ..... 113, 114

*To be argued by*
GEORGE TROSK.

# Supreme Court of the United States

**October Term, 1927**

THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy of Knauth, Nachod & Kuhne,

*Petitioner,*

*against*

THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO,

*Respondent.*

## *BRIEF FOR RESPONDENT.*

[Italics ours.]

Tersely stated, the questions involved in this case are:

1. Did the bankrupts, Knauth, Nachod & Kuhne (hereinafter referred to as "K. N. & K.") receive a certain remittance from the First National Bank of Trinidad, Colorado (hereinafter referred to as the "Claimant"), as the Agent of the Claimant to apply the same to a particular purpose; and

2. Independently of "1", was there an equitable assignment by K. N. & K. of certain moneys on deposit by them with Banca Commerciale Italiana (hereinafter referred to as "B. C. I.") for the payment of the draft held by Claimant?

The learned Special Master answered both questions in the negative (fols. 598-650). Claimant filed exceptions to his report (fols. 652-663) and, upon motion of the Trustee in Bankruptcy of K. N. & K., the learned District Judge overruled the exceptions and confirmed the report (fols. 667-673). Upon appeal to the United States Circuit Court of Appeals the order of the District Court was reversed and the proceeding remanded with instructions to grant the claimant a priority (fols. 772-777). That learned Court held (fols. 739-767) that K. N. & K. had made an equitable assignment of certain moneys which it had had on deposit with B. C. I. for the payment of the draft held by Claimant and, having so determined, found it unnecessary to consider whether the bankrupts had originally received the Claimant's money in a fiduciary capacity (fol. 769).

The case comes to this Court on a writ of certiorari.

Of the two questions presented, the Petitioner has chosen to discuss first the one involving the question of equitable assignment and, for that reason, we shall do likewise.

## THE FACTS RELATING TO THE QUESTION: WAS THERE AN EQUITABLE ASSIGNMENT BY BANKRUPTS OF CERTAIN MONEYS ON DEPOSIT BY THEM WITH B. C. I. FOR THE PAYMENT OF THE DRAFT INVOLVED IN THIS PROCEEDING?

The relations between K. N. & K. and the Claimant were governed by a written instrument prepared by K. N. & K. and known as their "Drawing Service" (Claimant's Exhibit 1, fols. 418-472).

This "Service" was inaugurated by K. N. & K. to enable their inland correspondents, of which Claimant

was one, to do a foreign exchange business without maintaining foreign balances. As K. N. & K. state in the foreword to their "Drawing Service" (fols. 418-419):

> "The constantly increasing demand for Foreign Exchange, on the part of the public, has lead progressive banks throughout the country to add the necessary equipment to their general banking arrangements to enable them to meet the requirements of their customers, in the matter of drafts and money order payments in foreign currencies. Inasmuch as the maintenance of a Foreign Department, involving the carrying of balances abroad, etc., is undesirable, from the standpoint of a majority of inland banks, we have aimed for many years to supply this want by extending to our correspondents the privilege of using our world-wide facilities for carrying on a foreign exchange business."

The *modus operandi* of the "Drawing Service" was this: K. N. & K. supplied their inland correspondents with a list of their foreign correspondents (Claimant's Exhibit "1," fols. 418-473) and with a book of "Foreign Drafts" (Claimant's Exhibit "2," fols. 473-480). Each page in the book of "Foreign Drafts" contained two forms, the upper a blank draft (fol. 478), and the lower, a form of "Advice." The pages were perforated so that each of these forms could be detached from a stub, as in the case of the ordinary check-book. When an inland bank was asked by one of its customers to issue a draft payable abroad, the bank would consult the "rate card," which was a list prepared and furnished each day by K. N. & K. to its inland correspondents, giving the rates at which K. N. & K. would "protect" drafts drawn that day on the various countries. This rate included, in addition to the foreign exchange value of the draft, a

sum fixed by K. N. & K. to compensate them for their service (fol. 70.) Thereupon in return for an amount fixed according to such rate, the inland bank would issue *its own draft* on one of the correspondents listed by K. N. & K. in their "Drawing Service," by filling out one of the forms in the book of "Foreign Drafts," detaching it from the book and delivering it to the purchaser. The bank would then fill out an "Advice" contained in the book of "Foreign Drafts," detach it from the book and immediately mail it to K. N. & K. with sufficient funds, computed at the rate fixed by K. N. & K. in their Rate Card, for the drawing of the draft on that day.

The draft and the "Advice" involved in this proceeding are Claimant's Exhibits "3" and "4" (fols. 481-483). The draft was for 24,360 Lire, drawn by Claimant on B. C. I., Sassari, Italy, in favor of Zara Sanna Giovanni.

The "Advice" mailed by Claimant to K. N. & K. immediately upon the sale of the said draft reads (fols. 482-483):

> "Pursuant to the terms and conditions governing your drawing service we have sold draft, bearing the above number, dated Trinidad, Colo., May 19, 1923.
>
> For Lit. 24,360.00 and shall thank you to protect same upon presentation.
>
> We remit herewith the sum of $1,191.20 @ rate quoted on Rate Card No. 18."

Claimant's check for $1,191.21, which accompanied the "Advice," was received by Bankrupts and deposited by them in their bank account.

The remission of this money to Bankrupts and the request "to protect" the draft upon presentation were in pursuance of the provisions of the Drawing Service,

by which the drawer bank, as principal, drew its drafts and advised K. N. & K. thereof, and by which K. N. & K. agreed

> "upon receipt of proper advices, and New York funds to cover such drafts at the rates quoted by us for the day on which the drafts are sold, our advices are at once forwarded and funds provided with the respective drawee banks for the payment thereof, by transfers of credit from our balance or otherwise." (See provisions of Drawing Service, fols. 419, 420).

Immediately upon receipt of the claimant's "Advice" and the check to cover, K. N. & K. notified B. C. I. of the drawing of the claimant's draft and directed B. C. I. to "honor" it, "charging the same to our account," and in another communication, sent at the same time, directed B. C. I. to charge the said draft "to the debit of our account" (Claimant's Exhibit 6 and 6D, fols. 487-489, 499-501).

The foregoing papers were received by B. C. I. on or before June 4, 1923 (fol. 76). They are known as Steamer Block "SS 8469-B."

It is stipulated that there was a regular course of dealing between the B. C. I. and K. N. & K., by which the B. C. I. sent to K. N. & K., approximately each week, statements of K. N. & K.'s account with the B. C. I. (fol. 78); that on these statements the B. C. I. would show K. N. K. the drafts advised which had been debited to K. N. & K.'s account since the preceding statement and that this practice of immediately debiting the bankrupt's account with these amounts was recognized as proper by the bankrupts (fols. 81, 82). Claimant's

Exhibit 8 is one of these statements of account, from which it appears that on June 4, 1923, B. C. I. debited K. N. & K.'s account with the total of Steamer Block "SS 8469-B," which included claimant's draft, and that it reported to K. N. & K. that it then carried for their account a specified balance, *being the sum which remained after deducting from their former balance various sums, including the amount of Steamer Block "SS 8469-B."*

Not only do the stipulated facts show that the money was taken *out of K. N. & K.'s account*, but they go further and show that these moneys, upon being taken out of K. N. & K's account, were credited to an account maintained by the B. C. I. entitled "Drafts Payable,"

> "in which account were also credited amounts of drafts advised to the said B. C. I. for payment by other depositors or clients of the B. C. I. in addition to the bankrupts" (fols. 89, 90).

No better statement of the nature and the purpose of the account to which these moneys were credited by the foreign bank could be made than that of the Trustee's witness, Mr. Dawson, Vice-President of the Guaranty Trust Company (fols. 339-340). Mr. Dawson said that he was familiar with the practices and usages in connection with the protection of drafts by New York bankers on behalf of inland banks (fols. 345-348); and

> "It is the universal custom, in every part of the world which I have visited or had banking relations with, that the drawee bank, upon receipt of advice from its client that a draft has been drawn on it, immediately charges the current account of that client with the amount of any draft or drafts and *sets it aside in a special fund awaiting the presentation of any drafts against that fund.*"

The "setting aside" is accomplished thus (fol. 349):

> "The practice is to charge the current account of the client with the sum of money and carry it over into another account which is known on the ledgers of most banks as 'unpresented drafts drawn,' where it is entered in a folio under the name of the bank whose account has been charged."

Once B. C. I. made the transfer to the "Drafts Payable" account,

> "no interest was allowed to the bankrupts or to anyone else upon the amount credited to the account termed, 'Drafts Payable,' as a result of advices from the bankrupts,"

although depositors were entitled to, and received interest from B. C. I. (fol. 92) on

> "the amount of the balance standing to their general credit."

In other words, this account was not in terms of K. N. & K. at all—it was an account in which B. C. I. kept track of what it recognized as "*its* commitments" (fol. 355).

The historical development of the practice shows, as the Trustee's witness testified, that originally the drawee banker, upon receiving notice that a draft had been drawn on him

> "held the money in his box or in his office, useless, awaiting the presentation of the committment or draft

and (fol. 372)

> *'probably earmarked each particular bag for a particular purpose'*

further, that this practice (fol. 357)

> 'has hung on in modern times • • • •'

except that now the foreign bank (fol. 365) accomplishes "*exactly the same result*" by making appropriate book entries, or, to put it another way (fol. 370).

> 'We still keep the money in the box, but not specifically. We look over our active liabilities which are imminent, and readjust our cash position in general, but not specifically.'"

Here, also, is a clear recognition that upon the receipt of an advice and the crediting of "Drafts Payable" the liability becomes "our liability", that is, *the liability of the drawee bank*.

**THAT K. N. & K. CLEARLY RECOGNIZED THIS IS CORROBORATED BY THE FACT THAT ONCE K. N. & K. ADVISED THE DRAFT, IT NO LONGER CONSIDERED THE AMOUNT ADVISED AS ONE OF ITS ASSETS (FOLS. 132, 156) AND K. N. & K. WARNED THEIR INLAND BANKS THAT THEY RECEIVED NO REPORTS FROM THE FOREIGN BANKS AS TO WHEN, OR WHETHER, DRAFTS ADVISED WERE EVER PRESENTED (FOL. 433)**

The Petitioner argues that the balance in the "Drafts Payable" account "still belonged to K. N. & K." (p. 33) because it was testified that moneys carried in that account were entered in a folio under the name of the bank whose account had been charged. The testimony referred to does not mean what Petitioner attributes to it. It means only that the usual cross-reference, common to all double-entry bookkeeping, was made, so that each item in the account could be traced to the source from whence it came.

The stipulated facts show further that while this fund was so set apart and held by the B. C. I. for the purpose

of meeting the claimant's draft, the receiver cabled B. C. I. (Claimant's Exhibit 10, fols. 520-521) that "all credit balances in favor of Knauth, Nachod & Kuhne, New York, must be held subject to my sole order."

It is interesting to note the response which this cablegram elicited from B. C. I. (Claimant's Exhibit 11, fols. 523-532). It enclosed a statement (Claimant's Exhibit 9, fols. 517-518), showing the state of K. N. & K.'s account up to the date of bankruptcy. This statement shows on its face that the amount of Steamer Block "SS 8469-B" had been charged out of the Bankrupts' account and had been credited to "Drafts Payable" on the books of B. C. I. *and that B. C. I. was indebted to the bankrupts only in the sum which remained after deducting from K. N. & K.'s former credit balance the amount of Steamer Block "SS 8469-B" and certain other Steamer Blocks advised by the Bankrupts.*

The next significant thing in Claimant's Exhibit 11 is B. C. I.'s notification to the Receiver that certain Steamer Blocks which had been advised by Bankrupts were (fols. 528-529)

> "being held in abeyance, not having been debited to the account *through lack of funds.*"

**THIS REFUSAL TO DEBIT K. N. & K.'S ACCOUNT WITH DRAFTS ADVISED "THROUGH LACK OF FUNDS" ESTABLISHES THAT THE CHARGING OF BANKRUPTS' ACCOUNT AND THE CREDITING OF "DRAFTS PAYABLE" WERE NOT MERE BOOK ENTRIES, BUT WERE INTENDED TO RECORD ACTUAL TRANSFERS OF FUNDS FROM ONE ACCOUNT TO ANOTHER.** On no other theory can the refusal of the B. C. I. to make the book entries on account of "lack of funds" be explained.

On June 29, 1923, the Receiver wrote B. C. I. (Claimant's Exhibit 14, fols. 536-538) requesting it to

> "rule off the account" of Knauth, Nachod & Kuhne on June 16, 1923, and to forward to him by return mail "a statement of their account up to that date, *as well as* a list of all unexecuted cable transfers and unpaid drafts and money orders * * *."

which again indicates that in the mind of the Receiver, when he sent this letter, "a statement of the *bankrupts'* account" on June 16, 1923, would *not* include moneys which had been set aside by B. C. I. to meet drafts theretofore advised to it by Bankrupts.

On August 23, 1923, the Receiver cabled B. C. I. to (Claimant's Ex. 18, fol. 552)

> "*cancel all drafts* charged but not paid before receivership and remit balance for (our) my credit to Central Union Trust Co., New York."

On September 10, 1923, B. C. I. wrote the Receiver another important letter (Claimant's Exhibit 19, fols. 553-558).

In the first place it confirmed a letter sent to the Receiver on September 8, 1923, which the Trustee has not produced.

In the second place it gave a resumé of certain enclosures (Claimant's Exhibits 19A and 19B, fols. 559-563) showing the condition of the Bankrupt's account and explaining how the fund returned to the Receiver was made up.

Claimant's Exhibit 19B, one of the enclosures in Exhibit 19, was a statement showing a balance in the bankrupts' favor of 1,629,770 lira. This statement and the letter in which it was enclosed show that in arriving at this balance, B. C. I. had accepted the Receiver's direction to "cancel all drafts charged but not paid before receivership" and had thereupon recredited to the ac-

count of the bankrupts the sum of 1,526,048.48 lira, *which sum represented certain specified amounts theretofore taken out of K. N. & K.'s account and credited to Drafts Payable to meet specified drafts advised.* A detailed statement of the drafts, the amounts of which were so recredited, was also enclosed in this letter and is Claimant's Exhibit 19A. This shows (fol. 560) that among these drafts *is draft 61161, the draft involved in this proceeding.*

It is stipulated that the amount reversed from the Drafts Payable account upon the Receiver's aforesaid direction was returned to the Receiver by the payment of its equivalent in dollars, to wit, $67,548.06 (fol. 111).

The petitioner asserts as emphatically as type will permit (p. 46) that the fact that B. C. I. honored the Receiver's direction to return the moneys in the Drafts Payable account is the strongest evidence that the moneys credited thereto were not appropriated to the payment of advised drafts. The following analysis of the evidence and of the Receiver's course with respect to that money, shows how definitely he recognized the contrary:

Mr. Dawson, the Trustee's expert on the customs governing the Drawing Service, was asked (fol. 350):

> "Is there * * * a general practice or custom with respect to the cancellation of advices, after their receipt by the foreign bank and prior to the presentation of the draft for payment?"

He was very cautious in his answer. First he asked to have the question repeated; then he answered (fol. 351):

> "Yes, there is a custom."

He was asked

"What is that custom?"

and he answered (fol. 351):

> "*I take it the question means when the drawer bank wants to cancel a draft that has already been drawn and advised.*"

The Trustee's counsel, who was examining, said (fol. 352):

"Precisely"

meaning that he limited his question to the custom with respect to the cancellation of advices in cases mentioned by the witness, to wit: "*Where the drawer bank wants to cancel a draft that has already been drawn and advised.*" Whereupon the witness answered that the custom was (fol. 352):

> "A communication of the fact of cancellation by any means he can avail himself of, cable, letter or anything else. Upon receipt by the drawee bank that such **DRAFT HAS BEEN CANCELLED**, a reversal entry is passed, taking the amount of such cancelled draft from the Unpresented Draft Ledger and crediting it back into the current account."

Mr. Dawson was the Trustee's witness and doubtless knew that they hoped to establish by him that, as Mr. Goldmark *originally* put it (fol. 350) there was

> "a general practice or custom with respect to the cancellation of *advices*."

Yet he refused to answer the question put to him in the affirmative—instead, *he first limited the question by making it clear that he treated it as referring only to*

*cases in which "the drawer bank wants to cancel a draft that has already been drawn and advised"* and *then* he answered that in *such* cases there was a custom. Of course, if "the drawer bank" was one of the banks using the Drawing Service, it would notify K. N. & K. that it "wants to cancel a draft that has already been drawn and advised," and thereupon K. N. & K. would send the foreign bank a notice to cancel the same. The reason the notice would be sent by K. N. & K. and not directly by the inland bank to the foreign bank was, as Mr. Dawson explained, because the foreign bank dealt with K. N. & K. in the transaction and had received the original notice of the drawing of the draft from K. N. & K. (fol. 353). This is not only Mr. Dawson's testimony, but is corroborated by the testimony of K. N. & K.'s auditor (fols. 282-284) and by the stipulation in the case (fol. 379):

> "Subject to proof to the contrary (of which none was offered), it is conceded that in every case (in which K. N. & K. sent notice of cancellation of a draft) the notification by the bankrupts to Banca Commerciale Italiana, *was preceded by a notification from the drawer bank that the draft had been lost or would not be presented to the drawee bank for payment, but in the case at bar no such notification was given by the drawer bank to bankrupts.*"

**WHEN THE RECEIVER, PROMPTLY AFTER HIS APPOINTMENT, INSTRUCTED B. C. I. TO HOLD "ALL CREDIT BALANCES IN FAVOR OF K. N. & K." SUBJECT TO HIS ORDER (CLAIMANT'S EXHIBIT 10), B. C. I. NOTIFIED HIM OF THE AMOUNT OF K. N. & K.'S BALANCE BY A LETTER WHICH SHOWED THAT B. C. I. DID NOT REGARD MONEYS WHICH HAD BEEN CREDITED TO THE "DRAFTS PAYABLE" ACCOUNT, TO COVER DRAFTS ADVISED, AS ANY PART OF K. N. & K.'S BALANCE (CLAIMANT'S EXHIBIT 11).**

**THEN, IT WAS, THAT THE RECEIVER ADOPTED ANOTHER MEANS TO GET THOSE MONEYS. THE CUSTOM BEING THAT THEY WOULD BE RE-CREDITED ONLY IF THE DRAFTS WERE CANCELLED, HE PROCEEDED TO INSTRUCT B. C. I. TO CANCEL THEM, DESPITE THE FACT THAT, UNDER THE UNIVERSAL CUSTOM, SUCH A NOTIFICATION COULD PROPERLY BE GIVEN ONLY IF THE DRAWER BANK HAD FIRST REQUESTED IT, AND THE DRAWER IN THIS CASE HAD NEVER MADE ANY SUCH REQUEST.**

What right the Receiver had, without Claimant's permission, to cancel a draft drawn by it, on which K. N. & K.'s name nowhere appeared, no one has ever attempted to explain.

The foreign bank was, of course, familiar with the custom governing the right to cancel drafts and knew that it existed only in cases where "the drawer bank wants to cancel." Consequently, when it received a notification from K. N. & K.'s representative *to cancel a draft* drawn by an inland bank, it assumed, as it had a perfect right to do, that the condition precedent to such notification existed, to wit, that "*the drawer bank* wants to cancel." Thereupon it recognized the notification, cancelled the draft and reversed the entry. In doing so, however, it cannot by any process of reasoning be claimed that B. C. I. recognized the right of the Receiver to procure a reversal of an entry in the "Drafts Payable" account by giving notice of the cancellation of a draft where the drawer had *not* requested the cancellation.

We earnestly submit that a clearer case of an equitable assignment in claimant's favor than that shown by this record would be difficult to find.

## POINT I.

**Pursuant to the terms of the drawing service, K. N. & K. caused Banca Commerciale Italiana to create, out of K. N. & K.'s funds on deposit with Banca Commerciale Italiana, a fund for the payment of the draft involved in this proceeding. Thereby an equitable assignment of the moneys was effected.**

Equitable assignment is a matter of intention, to be determined from the circumstances of the case and the acts and declarations of the parties. An intent on the part of a creditor to have his debtor set aside and appropriate, for the benefit of a third party, a portion of the funds of the creditor in the hands of the debtor, followed by an actual appropriation by the debtor at the creditor's request, as was the case here, results in an equitable assignment in favor of such third party.

In determining the obligation of K. N. & K. and their intention in advising the drafts abroad, it is essential to bear in mind certain provisions of the Drawing Service to which we do not think the Petitioner has called attention.

The "Drawing Service" provides, under the title "Terms and Conditions Governing the Use of K. N. & K. Drawing Service" (fol. 422):

> "Upon receipt of advice of draft, accompanied by adequate funds payable at par in New York, we shall promptly forward our advice of the same and provide the drawee with funds sufficient for the payment of the draft abroad, by a transfer of credit from our balance, or otherwise, * * *

> *Under this arrangement, our correspondents in this country act as* PRINCIPALS, *and issue drafts in their own names, our name not appearing thereon. In other words, we are* **EMPLOYED** *merely* **AS THE AGENTS OF THE DRAWERS** *for the purpose of advising the issue of their drafts and providing the drawee banks with sufficient funds to cover their payment.*"

On the cover of the book of "Foreign Drafts" which K. N. & K. distributed to inland banks for use in conjunction with the Drawing Service, they said (fols. 474-475):

> "*Under this arrangement our correspondents draw drafts for their own account as principals and our name does not appear, our sole function being to advise the drawees of the issue of drafts drawn by our correspondents and to provide for payment,* **IN WHICH FUNCTION WE ACT AS AGENTS OF THE DRAWERS.**"

In short, K. N. & K., recognizing the need of inland banks "to meet the requirements of their customers in the matter of drafts and money order payments in foreign currencies," invited these banks "to issue drafts in their own names" on correspondents of the bankrupts abroad and offered, as "employees and agents of the drawers," to advise the drawees of the issue of drafts drawn "and to provide for payments." This agency they undertook upon condition that there was first remitted to them a sum sufficient to cover the amount of the draft and an additional amount representing their compensation (fol. 70). They recognized that the Claimant would draw a draft payable in Italy and that it would be necessary *for the Claimant* to provide the foreign bank

with money with which to pay the draft it had drawn. This the Claimant could do in one of two ways. It could either *personally* provide the drawee bank with the money to pay the draft, or else it could engage *someone else* to do so for it. K. N. & K. held themselves out as peculiarly well fitted to act as Claimant's agent for this purpose. They stated that if the necessary funds were sent to them, they would notify the drawee bank of the drawing of the draft and, as Claimant's agents, "provide for the payment thereof." They undertook to perform *for the Claimant* a "function" which the Claimant would otherwise have had to perform itself, to wit: *put into the hands of B. C. I. the money which the Claimant would provide for the purpose of meeting the draft which the Claimant had drawn.*

The agreement to put this money into the hands of B. C. I. was not merely an agreement to transfer a credit at any time K. N. & K. might find convenient prior to the presentment of the draft. The Drawing Service expressly requires the fund to be created immediately upon the receipt by K. N. & K. of the advice from the inland bank accompanied by the necessary funds to cover. The Drawing Service provides fol. 420) that

> "*Upon receipt of proper advices*, and New York funds to cover such drafts at the rates quoted by us for the day on which the drafts are sold, our advices are *at once* forwarded and funds provided with the respective drawee banks for the payment thereof, by transfers of credit from our balance or otherwise."

and at folio 422:

> "*Upon receipt of advice of draft*, accompanied by adequate funds payable at par in New York,

> we shall *promptly* forward our advice of the same and provide the drawee with funds sufficient for the payment of the draft abroad * * *."

It is, accordingly, incorrect to state, as the Petitioner persists throughout its Brief in stating, that K. N. & K. merely undertook that by the time the draft would be presented they would have a credit abroad with which to pay it.

Bearing in mind the nature of K. N. & K.'s undertaking, let us look at what they did in fulfillment thereof.

Immediately upon receipt of claimant's advice that the draft had been drawn, accompanied by sufficient funds to cover the same, K. N. & K. notified B. C. I. of the drawing of the draft, directed B. C. I. to honor the same and charge it against its account. B. C. I. did as directed; it charged the account of K. N. & K. with the amount of the draft, and the amount so charged was immediately taken out of the K. N. & K. account and put into an account maintained by B. C. I. for the payment of drafts advised. This account included, as the stipulation admits, not only moneys appropriated for the payment of drafts drawn under the K. N. & K. Drawing Service, *but moneys appropriated for the payment of drafts drawn by others as well. The Bankrupts had no rights in the moneys in that account—they were held by the foreign bank "in a special fund" to accomplish "exactly the same result" as was originally accomplished by "earmarking each particular bag for a particular purpose" and putting it aside "in a box" to "await the presentation of the draft"* (fols. 348, 356-357, 369-370, 372). Once the money was taken out of K. N. & K.'s account, they ceased to regard it as one of their assets (fols. 132, 156) and they ceased to receive interest on it, although

they did receive interest on the moneys which *were* in their account; furthermore, they were not concerned with whether the draft was ever presented or not and B. C. I. never reported to them on that subject (fols. 160, 161, 433).

In reporting to K. N. & K. with respect to the amount of its balance in its hands, B. C. I. showed K. N. & K., by its statements, that it did not treat as any part of K. N. & K.'s balance in its hands, the moneys which had been taken out of the account and credited to the Drafts Payable account. This practice, it is stipulated, was proper. K. N. & K. had no rights in that money, except that if the drawer of the draft should request its cancellation (*which was not the fact here*) K. N. & K. would have the right, upon so notifying the foreign bank, to a reversal of the entry (fols. 350-352).

The Receiver with full knowledge that the Claimant had not asked to have its draft cancelled, and knowing, as he must be charged with knowing, that he had no right to cancel claimant's draft, sent notice of cancellation thereof to B. C. I. and thereby contrived to get possession of this money, which did not belong to the bankrupts, and which is, accordingly, no part of the bankrupt estate. The moneys returned are earmarked by the Exhibit which explains how they are arrived at and which shows that *they include the very money which had been set aside to pay the draft here involved.* The claimant as the holder of that draft is the owner of this money and is entitled to reclaim it.

*Coates* v. *First National Bank of Emporia*, 91 N. Y. 20;

*Risley* v. *Phoenix Bank*, 83 N. Y. 318;

*Throop Grain Cleaner Co.* v. *Smith*, 110 N. Y. 83;

*Rivers* v. *A. & C. Wright Co.*, 43 Southeastern, 499;

*Muller* v. *Kling*, 209 N. Y. 239;

*Fourth St. National Bank* v. *Yardley*, 165 U. S. 634;

*Fortier* v. *Delgado & Co.*, 122 Fed. 604.

The case of *Coates* v. *First National Bank of Emporia*, 91 N. Y. 20, is a leading authority in New York. The facts were as follows:

The First National Bank of Emporia, Kansas, was a depositor in the Mastin Bank of Kansas City. Both the Mastin Bank and the First National Bank were depositors in the bank of Donnell, Lawson & Co., in New York City. On July 30, 1878, the First National Bank of Emporia, having then more than $5,000 on deposit in the Mastin Bank, directed the Mastin Bank, by letter, to remit $5,000 to Donnell, Lawson & Co. "for our account; credit and charge our account." On August 1st, the Mastin Bank received this letter and acknowledged it, advising "We remit $5,000 to Donnell, Lawson & Co., New York, to your credit." The Emporia Bank, upon receipt of the letter, credited the Mastin Bank with $5,000 and charged that amount to Donnell, Lawson & Co. On August 1st, the Mastin Bank mailed to Donnell, Lawson & Co., a paper reading

> "Pay to the order of credit, the First National Bank, Emporia, Kansas five thousand dollars.
> To Donnell, Lawson & Co."

accompanied by a letter to Donnell, Lawson & Co. to the effect that they would find enclosed, for the credit of the

Emporia Bank, $5,000. On mailing this letter the Mastin Bank charged $5,000 on its books to the Emporia Bank and credited that amount to Donnell, Lawson & Co.

Two days after these transactions the Mastin Bank assigned to the plaintiff.

Donnell, Lawson & Co. received notice of the assignment by telegraph from plaintiff August 5, 1878, and on the same day, a little later, the letters and orders above mentioned were received by them.

The plaintiff, as assignee of the Mastin Bank, demanded payment of the balance appearing to be due to the Mastin Bank at the date of the assignment. The defendants also demanded payment of the orders. Donnell, Lawson & Co. paid into court the full amount of the apparent credit and thereupon the defendants were substituted in their place as defendants.

The object of the suit was to determine the title to this fund.

The Court said:

> .. • • • It seems to be well settled that a mere check or draft does not operate as an assignment or appropriation of the drawer's deposit in favor of the payee before acceptance by the bank (*Harris* v. *Clark*, 3 N. Y. 93; *Atty. Genl.* v. *Continental Life Ins. Co.*, 71 id., 325; 27 Am. Rep., 55), but the doctrine has not been extended beyond instruments of that character, drawn in the ordinary form; nor to a transaction not restricted to the very terms of such paper. • • •
>
> "I am unable to see why, on the first day of August, there was not a complete and consummated contract between that bank and the Mastin Bank. The Mastin Bank, up to that day, owed the Emporia Bank, and was requested to pay its debt by transferring funds then with Donnell, Lawson

& Co. They say by letter, 'we will do so,' at once charge the Emporia Bank, and credit themselves with $5,000; on the same day, by letter, they inform the Emporia Bank that this has been done, and in fact they direct Donnell, Lawson & Co. to 'pay to the order of credit, the Emporia Bank,' the sum named. The Emporia Bank also credited the Mastin Bank with it. These circumstances in the conduct of both parties establish an agreement, the effect of which, as between the Mastin Bank and the Emporia Bank, was 'to estop the former from setting up that so much of the credit to which they were before entitled from Donnell, Lawson & Co. did not belong to the Emporia Bank, and the Emporia Bank from saying that so much of the debt before due from the Mastin Bank to it had not been extinguished. (*Allen* v. *Culver*, 3 Den., 284 292). Written out, the contract indicated by the bank entries and the correspondence is one of assignment of so much of the credit, or funds then to its credit with Donnell, Lawson & Co., to the Emporia Bank, and a discharge of a debt due by it to that bank. *The whole was completed the moment the letter of the Mastin Bank to the Emporia Bank was placed in the post office.* • • •

"Nothing further remained to be done. • • • As between these parties the credit or funds had ceased to be the property of the Mastin Bank. The Emporia Bank was no longer creditor, because it was paid. The credit, or right to call upon Donnell, Lawson & Co. for the same amount, was the means of payment. • • •

"• • • Here by the act of the customer, the title to the account itself had passed from him, and the check, or order, as it may more properly be called, was, between the customer and the assignee —the Emporia Bank, of no importance. *The bankers, by virtue of the assignment, owed the money specified in the account, to the Emporia Bank, and it was not a matter as to which they had any discretion to exercise.* • • • "

The Court after citing *Burns* v. *Carvalho*, 4 M. & C., 690, a leading English case, continued:

> "In the case before us, as in that, there was an existing fund in the agent's hands and a distinct contract by the debtor with its creditor, to discharge the liability out of that fund, and to give directions for that purpose. * * *
>
> "I have not overlooked the contention of the respondent that the entries were mere matter of bookkeeping for the convenience of the bank. It might be so if they stood alone. But taken in connection with the letters between the parties, and the order and letter of advice sent to Donnell, Lawson & Co., they are equivalent to an actual transfer of credit, or account; to an assignment, therefore, at least in equity, of the fund in the hands of Donnell, Lawson & Co. * * *
>
> "In *Pratt* v. *Foote* (9 N. Y. 463) the plaintiff, a private banker, was held charged as on an agreement by entries made in the books of his bank, although not communicated to the defendant, and the latter was relieved from an obligation by reason of them. *In the case before us the entries were preceded by the letter of the Emporia Bank, requesting a transfer of credit, accepted by the Mastin Bank, and the books made to conform thereto. Taken together they conclude the Mastin Bank and of course its voluntary assignee.* * * *
>
> "It follows that the fund did not pass to the assignee. (*Hopkins* v. *Banks*, 7 Cow. 650; *Muir* v. *Schenck, supra; Osborn* v. *Thomas*, 46 Barb. 514). The assignment to him is dated August 3; it purports to transfer the property 'and credits' of the Mastin Bank; of course it speaks as of the day of its date, *and on that day the credit in question was not its property. It could not withdraw or change its application and so revive its indebtedness to the Mastin Bank, or that of the defendants to itself.* It does not appear, however, that the Mas-

> tin Bank undertook to again deal with this fund, or to assign it to its trustee, nor, if it had been possible to do so, that it undertook to deprive the defendants of the benefit of the contract under which they claim. It follows from these observations that the learned referee erred in finding that the money in question passed by assignment to the plaintiff, and that the defendants were not its owners."

The learned counsel for Petitioner argues (Petitioner's Brief, p. 55) that the basis of the decision in the *Coates* case was

> "that from all the circumstances of the case, it was concluded that the intention of the parties had been presently to assign a specific existing fund in another bank and that the delivery of the checks was simply the means of enabling the assignee to collect the assigned funds."

He overlooks that whether an assignment was intended is always a matter to be determined from the "circumstances of the case" and that "the circumstances of the case," from which the intention was gleaned in the *Coates* case, were even less cogent than those at bar. If "the circumstances of the case" in *Coates* v. *First National Bank* reflected an intention to assign a fund, then we submit the circumstances of the present case certainly reflect such an intention.

The case of *Muller* v. *Klug* (209 N. Y. 239) is important because of the similarity of the facts to those in the case at bar. In that case the firm of Scholtz, Sanchez & Co. of New York, defendant's assignor, requested the plaintiffs to purchase a draft drawn by them upon Demachy & Seilliere of Paris for $7,000. As an inducement to the plaintiffs to purchase the draft, Scholtz, Sanchez

& Co. showed them a letter of Demachy & Seilliere in which letter Demachy & Seilliere promised to accept drafts drawn upon them by Scholtz, Sanchez & Co. up to the limit of 250,000 francs, upon the security of drafts drawn by Scholtz, Sanchez & Co. upon one Invernizio of Tortona, Italy, to be furnished therewith. Scholtz, Sanchez & Co. informed the plaintiffs that they would secure the draft upon Demachy & Seilliere by sending to Demachy & Seilliere another draft drawn upon the said Invernizio for $7,000 and that Invernizio was then indebted to Scholtz, Sanchez & Co. in that amount. The plaintiffs purchased the draft and paid Scholtz, Sanchez & Co. therefore. The draft was in the form of a bill of exchange drawn on Demachy & Seilliere, payable to plaintiff sixty days after sight, for 35,000 francs. To secure Demachy & Seilliere for the acceptance and payment of the said draft, Scholtz, Sanchez & Co. sent them a draft on Invernizio with a letter in which they stated that they had drawn "against this remittance" in favor of the plaintiffs. The plaintiffs sent their drafts to their correspondents in Paris, but before it reached there, Scholtz, Sanchez & Co., the drawers, had failed. Demachy & Seilliere learning of the failure, refused to accept the draft, and returned to defendant the draft on Invernizio. Claims were then made by plaintiffs and by defendant, as assignee of Scholtz, Sanchez & Co. upon Invernizio. Defendant was allowed to collect, under an agreement to submit to the Court the question as to who was entitled to the proceeds. The Court, through Judge Gray, held that:

> "* * * The facts furnished the inference, irresistible as it seems to me, that Scholtz, Sanchez & Co. intended, and that the plaintiffs understood,

that a debt, or part of an indebtedness, owing by Invernizio to the former, was to be transferred, and ultimately paid, to Demachy & Seilliere, as a fund to cover the payment of the draft upon them. Summarily stated, the transaction was that the plaintiffs purchased the draft on the French firm, upon the drawers exhibiting to them, to induce the purchase, a letter of the French firm, in which they promised to accept drafts, up to a certain limit, 'upon the security of drafts drawn by Scholtz, Sanchez & Co. upon Invernizio, to be furnished therewith;' the drawers, at the time, informing the plaintiffs that they would secure their draft on Demachy & Seilliere, by sending to that firm another draft drawn by them on Invernizio for the same amount against an existing indebtedness of Invernizio, upon an account for goods sold. Had the transaction been effectuated, as intended and understood when entered upon, there would have been a substitution of the liability of Invernizio to Demachy & Seilliere for that of Scholtz, Sanchez & Co. The purpose of the transaction, plainly enough, was to facilitate the collection of the money owing by Invernizio in account. The question is whether, as between the plaintiffs and the general creditors of Scholtz, Sanchez & Co., the equities of the former are superior. The defendant stands in the shoes of Scholtz, Sanchez & Co.; with no greater rights, as against the plaintiffs, than his assignors possessed. • • • I think that the circumstances attendant upon the purchase disclosed that *the plaintiffs had parted with their money on the supposed security of a fund, to be created by the transfer of the drawers to the drawees of the debt owing by Invernizio. In transactions of such a nature, the surrounding circumstances are to be considered by a court of equity in determining the intention of the parties.* • • •

"• • • *Any act, which makes an appropriation of a fund, amounts to an equitable assignment of it* (Story's Eq. Jur., sec. 1047). In my opinion, the circumstances do justify us in giving such a construction in the present case. If, from what took place, the inference is to be drawn that the parties intended that the plaintiffs should be entitled to the security of the drafts on Invernizio, I think a court of equity might give effect to the intent by holding that there was an equitable assignment of the debt it was drawn against. Such a construction, to use the language of Judge Finch in *Tallman v. Hoey* (89 N. Y. 537), when speaking upon the subject of equitable assignments (p. 539), 'proceeds upon a necessity demanded by the justice of the case, and to obviate an injury, or a wrong, which would otherwise occur. Where the holder (of a bill) has parted with nothing, and so loses nothing by the application of ordinary legal rules, no pressure of justice requires the intervention and the help of an equitable doctrine.' Whatever may be the doubt as to the application of this equitable rule, I think there should be no doubt that the plaintiffs' case is safely within the equitable doctrine that, *where the just and clear rights of a party to payment of a debt from a particular fund can be secured in no other way, the fund, or its proceeds, will be regarded as a trust for his better security.*" • • •

"• • • I think, under the circumstances surrounding the negotiation of the sale of the draft to the plaintiffs, that the defendant took over the moneys, in question, as a fund charged with a trust for its application to their claim and that the general creditors have no equal right thereto."

In *Fourth Street Bank* v. *Yardley* (165 U. S. 634), the Supreme Court of the United States, citing *Ketchum*

v. *St. Louis*, 101 U. S. 306, *Risley* v. *Phoenix Bank* and *Coates* v. *First National Bank, of Emporia*, says (p. 644):

> "Whilst an equitable assignment or lien will not arise against a deposit account solely by reason of a check drawn against the same, yet the authorities establish that if, in the transaction connected with the delivery of the check it was the understanding and agreement of the parties that an advance about to be made should be a charge on and be satisfied out of a specified fund a court of equity will lend its aid to carry such agreement into effect as against the drawer of the check, mere volunteers, and parties charged with notice."

The Petitioner's only comment upon *Muller* v. *Kling* and *Fourth Street Bank* v. *Yardley*, *supra*, is that there were in those cases (Brief, p. 55)

> "the intention equitably to assign a specific obligation—the intention to contract respecting a specific *res*."

This merely begs the question. We are all agreed that equitable assignment is a matter of intention. The cases we have cited are cases in which the Courts have found, from circumstances not even as persuasive as those present here, that the intention to create an assignment was evident. If such an intention was found to exist upon the facts in those cases, that intention is certainly discernible from the facts here.

The Court of Appeals of the State of New York has recently stated the test which it will apply to determine whether there has been an equitable assignment.

*Huskie Iron Co.* v. *Korn*, 229 N. Y. 179.

In that case Judge Collin, speaking for the Court, said (p. 183):

> "The test of an equitable assignment is the inquiry whether or not an assignment makes an appropriation of the fund so that the debtor would be justified in paying the debt or the assigned part to the person claiming to be the assignee. (*Fairbanks* v. *Sargent*, 117 N. Y. 320; *Williams* v. *Ingersoll*, 89 N. Y. 508; *Jones* v. *Mayor, etc., of New York*, 90 N. Y. 387; *Lowery* v. *Steward*, 25 N. Y. 239; *Holmes* v. *Evans*, 129 N. Y. 140.)"

If the foregoing test be applied, there can be no doubt that there was an assignment here. B. C. I. would have been not only "*justified*" in paying the claimant's draft; it was *expected* to pay it *and had actually set aside the money with which to do so.*

In *Jackson* v. *Tallmadge*, 216 App. Div. 100, the Court said (p. 102):

> "In Alexander v. Steinhardt, L. R. (1903) 2 K. B. 208, it was held that, where a debtor mailed instructions directing his agent to pay over certain moneys to a creditor, and also mailed a notice of the instructions to the creditor, the assignment was complete at the point of mailing and took effect, although before the mails arrived the debtor was bankrupt. The case is criticized by Prof. Williston, and declared unsound. Williston on Contracts, sec. 436, note. However, the law so declared appears to obtain in New York. Barry v. Equitable Life Assurance Society of United States, supra."

We submit that in reason, as well as upon the authorities, there was an equitable assignment here.

The Petitioner argues that if an assignment had been intended (p. 26) K. N. & K. would have set up a credit for Trinidad

> "so that when the draft was presented Trinidad would have a credit of its own on the B. C. I. books to which its draft could be charged."

Perhaps that method might have been employed but it was not the *only* method, nor does the failure to adopt *that* method indicate that some other method was not just as effective. K. N. & K. had no control over the foreign bank's internal bookkeeping procedure and was not interested in the manner in which the foreign bank made a record of its obligations. From the point of view of the foreign bank, however, the bookkeeping involved in carrying their obligations on drafts advised in the "Drafts Payable" account was much simpler than setting up a separate account in favor of each of the thousands of inland banks which might draw drafts under the Drawing Service and that is probably why this method was adopted.

The evidence shows that upon receipt of advice of the drawing of a draft, B. C. I. credited the necessary amount to the "Draft Payable" account and made appropriate notations to show that the sum so credited was to be applied to the payment of the particular draft (see fols. 508, *et seq.*). In crediting drafts advised to "Drafts Payable" account B. C. I. was creating an account which, in legal effect, was exactly the same as the special account usually maintained by a lawyer, in which he deposits collections made on behalf of his clients. He does not open a separate trust account for each client each time he makes a collection. He has one omnibus account in which he deposits all such collections. It is a trust account for the benefit of his clients to the extent that their funds respectively have been put into it. So it was with the "Drafts Payable" account of B. C. I. The moneys which

went into it they held for particular purposes, to wit: the payment of the various drafts noted in it. There was a trust in favor of the holder of each draft to the extent that money for the payment of that draft was in the account and the mere fact that this method was adopted in preference to opening separate accounts in favor of the respective drawer banks is of no greater significance than the lawyer's failure to open a separate trust account for each client for whom he makes a collection.

It is argued (page 31) that K. N. & K. gave "no directions" to B. C. I. to set up a fund which should be irrevocably appropriated to the payment of drafts

> "but simply directed them to protect the drafts to the debit of their (K. N. & K.'s) account and to honor the drafts, charging the same to their (K. N. & K.'s) account."

It is, of course, of no moment that "no directions" were given by K. N. & K. to B. C. I. "to appropriate" a fund in each case. It is conceded that the procedure employed between K. N. & K. and B. C. I. was a continuous and uniform one, pursuant (fol. 348) to "the universal custom." K. N. & K. knew what was being done and was satisfied with that procedure; indeed, *once it advised the draft abroad it no longer considered the amount advised as one of its assets* (fols. 132, 156-158). It received no interest on the money transferred and its interest in the transaction thereupon ceased to such an extent that it was not interested to know whether the draft was ever presented or not (fols. 160, 161, 433).

The Trustee continually asserts that the underlying intention of the Service was that the drafts drawn under it

> "should be treated just like a draft K. N. & K. itself had drawn."

This is a purely gratuitous interpretation of K. N. & K.'s obligation, supported by nothing in the record. The Petitioner argues (pages 22-23) that the references in the opening paragraph of the List of Foreign Correspondents to the world-wide facilities of K. N. & K. for carrying on a foreign exchange business (which involved the carrying of balances abroad) indicate that only a transfer of credit was contemplated. This conclusion does not follow from the premise. It is the very fact that K. N. & K. had balances abroad which put it in a position to provide funds abroad with greater facility than inland banks could, but the *means* which K. N. & K. would adopt to provide that fund were immaterial. They could use any means "recognized in financial circles" (*Leguiti* v. *Bank*, 230 N. Y. 415.).

The Petitioner seeks to avoid an equitable assignment by emphasizing the fact that K. N. & K. took the same steps in advising drafts drawn by them as they took with respect to drafts drawn by inland banks under the Drawing Service (Trustee's Brief, page 21). This circumstance is totally immaterial, as the Court of Appeals made clear in the *Leguiti* case, when they pointed out that although the acts performed by the banker in the "Sale of Credit" cases may be the same as the acts performed by him in the "transmission" cases, "*the practice of merchants and banks has recognized the difference; so have the Courts*" (230 N. Y., at page 421).

The Petitioner argues (Brief, page 32), that the entries made by B. C. I. were made by it as

> "a convenient method of indicating to the drawee banker what his commitments were likely to be in the immediate future and thus enabled him to have liquid and available for immediate use enough capital to meet those commitments."

The evidence disproves this statement. **B. C. I. DID NOT MAKE ENTRIES IN THE "DRAFTS PAYABLE" ACCOUNT UNTIL IT WAS PREPARED TO TREAT THE OUTSTANDING DRAFT AS ONE OF ITS OBLIGATIONS. THIS APPEARS FROM THE FACT THAT IN CASES WHERE DRAFTS WERE ADVISED AT A TIME WHEN K. N. & K. DID NOT HAVE SUFFICIENT FUNDS WITH B. C. I. TO COVER THE SAME, B. C. I. REFUSED TO CREDIT SUCH DRAFTS TO THE "DRAFTS PAYABLE" ACCOUNT (FOLS. 528-529).** If the "Drafts Payable" account had been merely a record of drafts advised, as distinguished from a record of drafts which the foreign bank undertook to *pay*, there would have been no reason for the refusal of the foreign bank to make the entries simply because K. N. & K. did not have a large enough bank account to cover them. Furthermore (fols. 305-308), it must not be overlooked that this "commitment" recorded in the "Drafts Payable" account, to which the learned counsel for Petitioner refers, was not a commitment to K. N. & K., but to a *stranger* and was a *new* relationship, undertaken by the foreign bank to the holder of the draft; that as Dawson, the Trustee's witness, testified, the moneys put into the "Drafts Payable" account are set

> "aside in a special fund awaiting the presentation of any drafts against that fund" (fol. 348)

and that the present method is used to accomplish "exactly the same result" (fol. 365) as was originally accomplished by the drawee banker by "earmarking each particular bag for a particular purpose" and putting

> "the money in a box in his office, useless, awaiting the presentation of the commitment or draft" (fols. 356-357).

## THE CASES CITED BY PETITIONER ARE NOT IN POINT.

### THE INTERBOROUGH AND THE NOYES CASES.

These cases are clearly distinguishable from the present case and the *Interborough* case expressly recognizes the distinctions and points out that the result there would have been different if there had been present some or all of the circumstances which are present in the case at bar. That case is an authority in the claimant's favor. It involved the relation of debtor and creditor between the corporation and its bank and merely held that where a depositor, for its own convenience, directs that a portion of its funds shall be carried *in its own name* and that *its own checks* for interest on its bonds should be charged against it, the bondholders acquire no trust in the deposit. *The court expressly recognized that if the creditor were told of the setting apart, and assented thereto, a different situation would arise* (288 Fed., p. 345), citing from *Story on Equity:*

> "* * * But if upon notice that creditors should assent thereto and no intermediate revocation should have been made by the assignor or remitter, there in equity the assignee or mandatary will be held a trustee for the creditors. * * *

> "* * * It may be revoked at any time before it is executed, or at least before any engagement is entered into by the mandatary with the third person to execute it for his benefit; and it will be revoked by any prior disposition of the property inconsistent with such execution. *But if no revocation is made and the mandate continues in full force, the trust as such continues for the benefit of such third person who after his assent thereto notified to the mandatary may avail himself of it in equity without any reference to the assent or dissent of the mandatary upon such notice; for his receipt of the property binds him to follow the orders of his principal.*"

In our case it was well understood between the parties that the fund would be created abroad. In fact the claimant entrusted the bankrupts with its money on the faith of the bankrupts' assurance that that would be done, the bankrupts, in their "Drawing Service" having agreed to

> "provide the drawee with funds sufficient for the payment of the draft abroad, by a transfer of credit from our balance, or otherwise"

and this obligation was actually carried out. Hence the foregoing quotation from the *Interborough* case applies. In the *Interborough* case the court pointed out that the money on deposit in the bank (p. 346)

> "was not received by the latter under instructions to distribute it among specified creditors, or to the coupon holders. It was received by the Empire Trust to be paid out on account checks to be drawn by the Interborough and directed to be charged against the separate account which had been created."

In our case there was no such situation. The money set apart by the Banca Commerciale Italiana was to be paid against the draft drawn by claimant and not upon any subsequent order of the bankrupts. In the *Interborough* case (p. 346) the court also quoted from the opinion of the court in *Adams* v. *Hackensack Improvement Commission*, 44 N. J. L., 638, as follows:

> "* * * The naming of a bank in a promissory note as the place of payment does not make the banking association an agent for the collection of the note or the receipt of the money. No power, authority, or duty is thereby conferred upon the banker in reference to the note; and the debtor cannot make the banker the agent of the holder by simply depositing with him the funds to pay it with. Unless the banker has been made the agent of the holder by the endorsement of the paper or the deposit of it for collection any money which the banker receives to apply in payment of it will be deemed to have been taken by him as the agent of the payer. 1 Daniel's Neg. Inst. 326; *Hills* v. *Place*, 48 N. Y. 520. *Such a deposit without some active appropriation by the banker, does not create any privity of contract as between the banker and the holder of the paper.*"

thereby recognizing the rule that *if the banker did do some act of appropriation, privity of contract as between the banker and the holder of the paper would result.* There certainly was an appropriation in our case.

The following principles were laid down as established by the court in the *Interborough* case (p. 347):

> "If A. places money in the hands of B., to be delivered to C., a trust arises in favor of the latter. The acceptance of the money with notice of its ultimate destination creates a duty on the part

of B. to devote it to the purpose intended, and a court of equity will enforce the trust. *McKee v. Lamon*, 159 U. S. 317, 322, 16 Sup. Ct. 11, 40 L. Ed. 165. In this instance also A. parted with control over the fund when he placed it in B.'s possession.

> "Every person who receives money to be paid to another, or to be applied to a particular purpose, to which he does not apply it, is a trustee, and may be sued either at law for money had and received, or in equity as a trustee, for a breach of trust"

thus recognizing the very rule for which we contend. The rule for determining whether a trust exists, as stated in 19 American and English Encyclopedia of Law, Second Edition, page 16, was adopted by the court in the following language (p. 349):

> "But a mere agreement to pay a debt out of a designated fund does not give an equitable lien upon the fund, or operate as an equitable assignment thereof. *There must be an appropriation of the fund protanto, either by giving an order, or by transferring it otherwise in such a manner that the holder is authorized to pay the amount directly to the creditor without the further intervention of the debtor.*"

In our case there was an appropriation of the fund, both by the giving of the order from the bankrupts to Banca Commerciale Italiana and by the transferring of the money by Banca Commerciale Italiana from the bankrupt's account to Banca Commerciale Italiana's Drafts Payable account, out of which the Banca Commerciale Italiana was

> "authorized to pay the amount directly to the creditor without the further intervention of the debtor."

The court further recognized the rule (p. 349):

> "* * * But it is now definitely settled in the Federal Courts that a promise based on a consideration to pay out of a particular fund creates a lien on the fund, which attaches to the fund when it comes into existence and which equity will enforce, holding the promisor to be a trustee as soon as he gets title. *Barnes* v. *Alexander*, 232 U. S. 117, 120, 121, 34 Sup. Ct., 276, 58 L. Ed. 530."

It is perfectly apparent from what has been said, that the *Interborough Consolidated Corp.* case is not only no authority against the claim of the claimant in this proceeding, but that in that case the court distinctly recognized that if there were present there some of the facts and circumstances which are present here, an equitable assignment would have resulted.

The Petitioner says that the Court below admitted the *Noyes* case to be "more nearly akin" to the present case "than any other" (p. 48). The Court below did no such thing. It said that the decision in the Interborough case was "quite remote" (fol. 763) and then said that the *Noyes* case was "more nearly akin"—meaning, of course, that it was closer than the "remote" *Interborough* case and not that it was closer than "any other" case.

The *Noyes* case held merely that where a corporation deposits its money in a special account *in its own name*, to meet interest coupons on *its bonds* as they become due, there is created merely the relation of debtor and creditor and the depository does not become a trustee in favor of the coupon holders. In that case the corporation opened a bank account designated by the bank "Chicago, Rock Island & Pacific Railroad Co., Coupon

Account," and transferred to this account a sum of money from the corporation's general account. The money still was in an account *in the depositor's name* and never ceased to be the depositor's money. In our case the money was taken out of K. N. & K.'s account and put into the foreign bank's own account, which it called "Drafts Payable," and which was a record of "its" obligations on drafts advised. This account, as Dawson testified, was the record of moneys set aside "in a special fund awaiting the presentation of any drafts against that fund." It was a fund which performed the same function as was originally accomplished by the drawee banker by putting "the money in his box or in his office" there to be held "useless, awaiting the presentation of the commitment or draft." Surely there is no analogy between such a fund and money which a depositor puts into his bank under circumstances like those in the *Interborough* and the *Noyes* cases. The distinction is, that although a fund may be designated as the fund *out of which* certain commitments will be paid, that fund does not become the property of the holder of the commitment *as long as the fund remains in the depositor's name and under his dominion.* As we have shown, the money in the "Drafts Payable" account was not the property of K. N. & K. K. N. & K. received no interest on it, although it did receive interest on its general balance; K. N. & K. did not treat moneys deducted from its account and transferred to the "Drafts Payable" account as an asset of K. N. & K. Once the money was deducted from its account, K. N. & K. had nothing further to do with it *and was not even interested in finding out whether it had been called for by the draft holders or not.* Furthermore, as we have also shown, K. N. & K. had no right

to revoke the drafts which were outstanding and procure a "recredit" to their account, except in cases where "the drawer bank wanted to cancel a draft," which was not the case here. All that happened in the *Noyes* and *Interborough* cases was that the depositor created an account *in its own name* and under its exclusive control and "authorized" or, as the court said in the *Noyes* case (180 A. D. p. 166) "permitted" the bank to pay coupons out of said account. There was no "segregation" *in favor of the holder of the commitment*. The money remained the depositor's and could have been withdrawn by the depositor at any time. Furthermore, the commitment which was to be presented *was a commitment of the depositor*. The commitment in our case was a commitment, not of K. N. & K. but a draft drawn by the claimant and payable by the foreign bank.

Erb v. Banco di Napoli, 243 N. Y. 45.

The Petitioner asserts this case is

> "indistinguishable from the present case."

In truth, it is totally different. The plaintiff possessed three coupons attached to bonds issued by the Kingdom of Italy. These bonds, as well as the coupons, provided that the coupons would be paid to bearer at the office of the defendant in the City of New York. Plaintiff's coupons fell into a trolley slot of a street railway and were lost and destroyed. The stipulated facts contained the statement that the Kingdom of Italy

> "has supplied the defendant with the funds wherewith to pay these coupons in the City of New York on their presentation and surrender to it, but not otherwise. Defendant is without authority from

> the Kingdom of Italy to part with said funds for or on account of such interest coupons, except on their presentation and surrender."

There is nothing in the opinion in that case to indicate that the money received by the defendant from the Kingdom of Italy was set apart in any special fund for the payment of the coupons or that these moneys were anything other than a part of the general bank deposit of the Kingdom of Italy with the defendant. In such circumstances, there is, of course, no assignment of the fund merely because the depositor has requested his banker to pay certain of the depositor's debts out of the moneys on deposit. As the Court of Appeals said at page 49, in adopting the language in an earlier case,

> "'The defendant has entered into no agreement to pay the bondholders, nor has it made any promise that it would pay them.'"

The situation in the present case is entirely different. Here, K. N. & K. asked B. C. I. to pay a particular draft, but the facts do not stop there as they did in the *Erb* case. The foreign bank acknowledged the instruction, took the money out of K. N. & K.'s account and put it into another account which, under the universal custom of the business, was recognized as an account in which the foreign bank kept a record of its own commitments to draft holders. This was done with the knowledge and approval of K. N. & K.

After pointing out that there had been no assignment of a particular fund from the mere direction to the banker to pay a debt out of a general deposit, the Court of Appeals said (p. 50):

> "There is, moreover, another reason why this suit cannot be maintained. While the relation

existing between a bank and its depositor, in a strict sense, is that of debtor and creditor, in discharging its obligation as a debtor, the bank must do so subject to the rule obtaining between principal and agent. It can pay out the money only in conformity to directions. (*Crawford* v. *West Side Bank*, 100 N. Y. 50, 53.)

The Italian Government gave directions to the Banco di Napoli, its depositary agent, 'to pay these coupons in the City of New York, on their presentation and surrender to it but not otherwise. Defendant is without authority from the Kingdom of Italy to part with said funds for or on account of such interest coupons except on their presentation and surrender.' I do not see how any court can modify these instructions so as to protect the bank in its accounting with its depositor. The plaintiff did not have her coupons to surrender."

Beecher v. Trust Co., 239 Mass. 48.

The Petitioner cites *Beecher* v. *Cosmopolitan Trust Company*, 239 Mass. 48 and *Erb* v. *Banco di Napoli*, 243 N. Y. 45, in support of its claim that the statement in the Drawing Service, that K. N. & K. would provide "sufficient funds" to cover, indicates that there was no intention to create an equitable assignment. The facts in the two cases cited distinguish them from the present case. In neither of those cases does it appear that the foreign bank, upon receipt of the advice, took out of the account of the advising bank the amount of the drafts charged and credited them to a separate account, such as the Drafts Payable Account in our case. Indeed, in the *Beecher* case it appears that before the advice was received by the foreign bank—indeed, on the same day that the advice was mailed from here—all further interference with the advising bank's account was enjoined

by notification of the Commissioner of Banks. The mere fact that the words "sufficient funds" were used in the *Beecher* case and that in the *Erbe* case (discussed *supra*, p. 40) the Court said that the Italian Government "had provided funds" cannot, upon the facts in those cases, make them precedents here. Neither can the fact that in some cases the words "protect" and "honor" were construed to mean merely an obligation to pay at maturity (Petitioner's Brief, pp. 23 26) be controlling here. Words, as this Court recently pointed out,

> "have no rigid and unchangeable significance. Their purpose is to express intention. They are not an incantation which unfailingly invokes agency. And the circumstances in this case indicate that they were here used with a different object." (*Equitable Trust Co.* v. *Rochling*, reported in New York Law Journal of November 29, 1927).

Likewise, the circumstances in this case indicate that the words "protect" and "honor" were not used merely in the sense of an obligation to pay at maturity. This is apparent when it is recalled that, by the terms of the Drawing Service, the claimant was invited to send its money to K. N. & K., as the Claimant's Agent, to perform a specified function, to wit: to protect the draft which the Claimant had drawn and, by the express terms of the agency, K. N. & K. agreed that upon receipt of the money (fol. 420)

> "our advices are *at once* forwarded and funds provided with the respective drawee banks for the payment thereof,"

or, as they put it in another place (fol. 422), upon receipt of the funds

> "We shall *promptly* forward our advice of the same and provide the drawee with funds sufficient for the payment of the draft abroad."

These are K. N. & K.'s own statements of the terms of their agency and they should not be permitted now to weaken their effect, to the prejudice of the Claimant which dealt with K. N. & K. upon the faith thereof.

### The decisions of the Circuit Court of Appeals in Matter of Zimmerman & Forshay and Ex Parte Muntean.

The learned counsel for Petitioner seeks to give the impression that there is some inconsistency between the decision of the Circuit Court of Appeals in this case and its decisions in *Matter of Zimmerman & Forshay*, 14 Fed. (2) 527 and *Ex Parte Muntean*, 13 Fed. (2) 730 (Petitioner's Brief, pp. 11-13). The decisions are perfectly consistent. In the *Zimmerman* case the Bankrupts sold the Appellant a Draft on a Bohemian Bank. On the same day they credited the drawee with the Draft on their books and advised it that they had so drawn. Prior to petition filed the drawee received the advice, charged the face of the draft against the bankrupts' balance on its books, and credited it to another account entitled "Drafts Payable". In these circumstances, as the Circuit Court of Appeals held, there was an actual transfer of the credit with bankrupts' consent and, consequently, an assignment of the fund. Our case is stronger than the *Zimmerman* case because there was no express proof there of an agreement between Zimmerman & Forshay and the foreign bank for the transfer of the credit on the drawee's books, whereas in our case the uncontradicted evidence is that there was a universal custom for the making of the transfer immediately upon the receipt of the advice of the drawing of the draft.

In the *Muntean* case, the distinction between that case and the present one was expressly pointed out by Circuit Judge Manton, who said (13 Fed. (2) 730, 732):

> "In Re Gubelman, Ex parte First National Bank of Trinidad, 13 F. (2) 732, handed down to-day, we decided the drawer, having taken up a draft drawn under the same 'service contract', stood in the position of an equitable assignee. It is true that this depended upon the drawer's subrogation to the holder's right, but the facts were not the same as here. There it appeared that before bankruptcy, the drawee had received the bankrupts' advice and had actually transferred the credit to the account of the draft. Here it appears only that the bankrupts had mailed the advice, and it does not even appear that they had an adequate balance with the drawee at that time or later."

### The Claim of Fidelity Trust Company of New York, amicus curiae.

Counsel for the Petitioner also asserts that there is conflict between the position of the Claimant here and of the *amicus curiae* Fidelity Trust Company of New York. There is no conflict between us. The position of the Fidelity Trust Company of New York differs from ours, as its Brief points out (p. 4), only in the fact that the foreign bank in its case did not charge the account of K. N. & K. and credit the Drafts Payable Account upon receipt of the advice; it merely sent a form letter acknowledging the receipt thereof. The Fidelity Trust Company of New York asks the Court to go further than it was necessary for the Court to go in deciding our case, by holding that the assignment was complete

> "when Knauth, Nachod & Kuhne, having received the moneys from the remitter, notified the drawee bank of the drawing of the draft and instructed it to pay the draft out of their moneys on deposit."

The Fidelity Trust Company of New York does not contend, as the Petitioner claims it contends (Petitioner's Brief, p. 14) that the assignment was in favor

> "not of the draft-holder, but of the drawer bank."

It expressly claims (its Brief, p. 8) that by their acts K. N. & K.

> "appropriated the funds abroad to the benefit *of the holder.*"

On pages 20, *et seq.*, of the Petitioner's Brief, is a statement of "The Necessary Results of Appellant's Contentions." With the apparent purpose of suggesting a *reductio ad absurdum*, the Petitioner has summarized our contention as resulting in the claim that upon the creation of the fund abroad, K. N. & K.'s responsibility for the application of the fund to the payment of the draft ceased.

In its brief in the Court below the Trustee sought to crystallize the same thought by putting the following question:

> "Does the appellant (Respondent here) seriously argue that the intention underlying the drawing service as agreed to by the parties was that the large and small banks scattered throughout this country who had no knowledge of foreign banks and bankers, were paying over their money to K. N. & K., relying on the credit, solvency and responsibility of foreign correspondents in scattered communities throughout Europe, wholly unknown to them and chosen by K. N. & K.?"

In our brief in the Court below we answered by putting the following question?

> "Does the Trustee seriously argue that the intention underlying the drawing service, as agreed to by the parties, was that K. N. & K., for the insignificant charge which it made, became guarantors of the continued solvency of all the large and small drawee banks scattered throughout the whole of the civilized world and that this guaranty was to remain in effect from the time of the drawing of the draft, through the period of its various negotiations and until the time of its ultimate presentation abroad, and that they were, during the same period, guarantors of performance by the foreign banks of their obligation to meet the draft when presented?"

It is interesting to observe that although the Trustee has carried much of its brief below into its present brief, it has not repeated the question it asked below.

To state the question put by the Trustee below is to answer it, because only one answer is conceivable. We have no hesitation in saying that in our opinion, under the terms of the Drawing Service, K. N. & K.'s obligation ceased the moment they put into the hands of the foreign bank a fund "sufficient to cover" payment of the draft and that they were in no respect responsible for the acts, omissions, derelictions, or defaults of the foreign bank thereafter. K. N. & K. had submitted a list of foreign correspondents. It made no representations as to their financial responsibility; that was a matter the inland banks could investigate before using any of them, if they chose. K. N. & K. agreed merely, as the *employee* and the *agent* of the inland bank, to provide the foreign bank with a fund equivalent to the one supplied to them

by the inland bank. K. N. & K. represented that they had better facilities for doing this than the inland bank itself had—*and that is the only reason the inland bank used K. N. & K. rather than send the currency direct.* The limit of K. N. & K.'s obligation was to provide the fund to the bank abroad—thereupon their responsibility ceased. They were not responsible for any acts or omissions of the foreign bank after that. It must be clear to the Court that any other interpretation of K. N. & K.'s obligation would make K. N. & K. the guarantor of the financial responsibility of every one of the hundreds of its scattered correspondents named in the list, as well as of their performance of their agreement to meet the draft when presented; furthermore, that this liability would be a continuing one throughout the indefinite, and, possibly, protracted period between the issuing of the draft and its presentation abroad. Considering the small fee which was paid for the service, it must be obvious that the inland bank did not expect K. N. & K. to assume, and K. N. & K. never intended to assume, such an obligation. Once the money was put into the hands of the foreign bank, K. N. & K. was "through"—so thoroughly through *that the foreign Bank never even advised what drafts had been paid and K. N. & K. were not interested to know* (fols. 160, 161, 433). The magnanimous offer by the Trustee to treat K. N. & K.'s obligation as one which continued "until payment was accomplished" cannot be considered seriously in view of the fact that K. N. & K. is in bankruptcy. The Court will not be slow to recognize that if K. N. & K. were *solvent* and the *foreign* bank had failed, K. N. & K. would be loud in their protestations against any such construction, and would forcefully and rightfully point to the terms of the Drawing Service, which show that K. N. & K. were but *employes* and *agents*

for a particular purpose; that they had performed the service for which they were employed, by putting into the hands of the foreign bank the fund which the inland bank gave them for that purpose and that thereupon they were discharged. Loudest of all would probably be the claim that it would be unreasonable to suggest that for the trifling fee paid K. N. & K. for their services, the inland bank expected, or that K. N. & K. undertook, to become guarantors, for an indefinite period, of the financial responsibility of every one of the hundreds of scattered correspondents named in the list and of performance by these correspondents. The trustee's contention that the inland banks did not rely upon the responsibility of the foreign banks because these banks "were chosen by K. N. & K." might, with equal logic, apply to the case of the lawyer who selects a name from one of the various law lists. If the trustee's contention is correct, the lawyer using one of these names would hold the publisher of the law list responsible for any omissions by a correspondent because the publisher had "chosen" the names in the list. No such responsibility has ever been suggested and it does not exist. The same is true of K. N. & K. with respect to the names in its list of foreign correspondents.

### *Conclusion with Respect to Cause of Action Based on Equitable Assignment.*

Claimant remitted money to K. N. & K. for the purpose of having K. N. & K., as Claimant's agent, transmit a fund abroad to pay a draft drawn by the claimant. K. N. & K. received this money and actually caused the fund to be created abroad. This is clearly established by the uncontradicted evidence, which shows that, pursuant to the regular, continuous and uniform practice which existed in the relations between K. N. & K. and B. C. I.,

(a) K. N. & K. NOTIFIED B. C. I. OF THE DRAWING OF THE DRAFT AND DIRECTED B. C. I. TO DEBIT THEIR ACCOUNT WITH THE AMOUNT THEREOF AND HONOR THE DRAFT;

(b) THAT THEREUPON K. N. & K. DEDUCTED THE AMOUNT OF THE DRAFT FROM THEIR BALANCE WITH B. C. I. ON THEIR OWN BOOKS AND NO LONGER TREATED THE AMOUNT SO DEBITED AS AN ASSET OF THEIRS;

(c) ONCE K. N. & K. ADVISED THE DRAFT ABROAD THEY WERE NOT THEREAFTER CONCERNED WITH WHETHER THE DRAFT WAS ACTUALLY PRESENTED OR NOT;

(d) IMMEDIATELY UPON THE RECEIPT OF THE ADVICE, B. C. I. DEBITED K. N. & K.'S ACCOUNT WITH THE AMOUNT OF THE DRAFT AND CREDITED ITS OWN "DRAFTS PAYABLE" ACCOUNT WITH A LIKE AMOUNT;

(e) IMMEDIATELY UPON DEBITING K. N. & K. AND CREDITING "DRAFTS PAYABLE," K. N. & K. CEASED GETTING INTEREST ON THE AMOUNT TRANSFERRED, ALTHOUGH IT DID GET INTEREST ON ITS BALANCES.

(f) THE "DRAFTS PAYABLE" ACCOUNT WAS AN ACCOUNT IN WHICH B. C. I. KEPT A RECORD OF ITS OWN COMMITMENTS ON DRAFTS ADVISED, "A SPECIAL FUND AWAITING THE PRESENTATION OF ANY DRAFTS AGAINST THAT FUND";

(g) THE "DRAFTS PAYABLE" ACCOUNT WAS NOT A MERE BOOKKEEPING CONVENIENCE BUT AN ACTUAL RECORD OF THE BANK'S COMMITMENTS, AS APPEARS FROM THE FACT THAT THE BANK REFUSED TO CREDIT "DRAFTS PAYABLE" WITH RESPECT TO ANY DRAFTS ADVISED UNLESS K. N. & K. THEN HAD A SUFFICIENT CREDIT BALANCE TO COVER THE SAME;

(h) EXCEPT IN CASES WHERE A DRAFT WAS CANCELLED, THERE COULD BE NO REVERSAL OF MONEYS CREDITED TO THE "DRAFTS PAYABLE" ACCOUNT AND K. N. & K. HAD NO RIGHT, AND HAD NEVER ATTEMPTED,

TO CANCEL A DRAFT ADVISED UNLESS THE INLAND BANK, THE DRAWER THEREOF, FIRST REQUESTED IT TO DO SO, AND

(i) NO SUCH NOTIFICATION WAS EVER GIVEN TO K. N. & K. WITH RESPECT TO, NOR DID THEY EVER ATTEMPT CANCELLATION OF, THE DRAFT INVOLVED IN THIS PROCEEDING.

These circumstances, we respectfully submit, make it perfectly clear that there was an equitable assignment by K. N. & K., out of their funds in the hands of B. C. I., for the payment of the draft involved in this proceeding. The receiver, long after bankruptcy, notified B. C. I. to "cancel all drafts advised but not paid before bankruptcy." Under the universal custom, as established by the trustee, this right existed only if the drawer bank had previously requested a notice of cancellation to be sent. The receiver had not received such a request and he therefore had no right to cancel the draft or to take the money which had been set aside for its payment. The money which was returned to him in consequence of this wrongful direction to B. C. I. is ear-marked. It came back with a communication identifying the particular drafts, the amounts of which had been credited to the "Drafts Payable" account and had, pursuant to the receiver's direction, been "recredited" to K. N. & K.'s account and returned to him. The draft involved in this proceeding was one of them and the money received by the receiver, which had been held by B. C. I. for the payment of this draft, and which had been "recredited" to K. N. & K. solely because the receiver wrongfully directed the cancellation of the draft, is the property of the holder of the draft, to wit, the Claimant herein.

The Trustee's suggestion that there is, or ever was, "vagueness" and "uncertainty" about Claimant's claim respecting the equitable assignment (Petitioner's Brief, p. 90) is a man of straw he has erected for his own purposes. Claimant has always claimed in the clearest terms, and still claims, that the assignment was an assignment for the benefit of the holder of the draft, whoever he might be.

## POINT II.

### The moneys remitted by Claimant to K. N. & K. were received by them in trust, as Agents of the Claimant, for a particular purpose.

Our Courts, Federal and State, have determined that where a banker sells, or agrees to sell, credit, whether it be represented by check, draft, money order or cable transfer, the consideration he receives therefor is not a trust fund. On the other hand, it is equally well settled that money received for a particular purpose is a trust fund, which the recipient holds in a fiduciary capacity.

With these distinctions, and their legal effect, in mind, the Petitioner has set out to give the transaction here involved a complexion which will fit it to the first class of cases because it is the rule applicable there that Petitioner would prefer to have applied here. The mere fact that in order to do so, the plain and unambiguous terms of the written agreement between the parties must be disregarded, to the great prejudice of the Claimant, which relied on it, seems to have presented no obstacle which the Petitioner is prepared to recognize.

The whole of the Petitioner's brief dealing with the relation resulting from the original transmission of the money to K. N. & K. is based on the premise that the parties did not intend to and, in fact, did not, assume the relation which the writing under which they operated expressly provides they should assume, to wit, that K. N. & K. should be (fol. 423)

> "employed merely as the *agents* of the drawers for the purpose of advising the issue of their drafts and providing the drawee bank with sufficient funds to cover their payment,"

or as stated in another part of the agreement (fols. 474, 475) that K. N. & K.'s "sole function" should be to advise the drawees of the issue of the drafts and to provide for payment *"in which function we act as agents of the drawers."*

It is claimed in the brief of the Petitioner (page 11) that the Claimant is not entitled to recover unless its rights be founded upon the intention of the parties, shown "without vagueness or uncertainty" and that the Claimant has failed to sustain that burden. To us it seems that the Claimant's right to reimbursement is shrouded neither in vagueness nor in uncertainty.

A great loss has been sustained and the question to be decided is: Who should, in justice, in equity, and in good conscience, bear the burden? The Claimant comes into Court and urges merely that the agreement, *couched in language chosen by the bankrupts*, should be held to mean *what it expressly says* and what they had a right to assume it meant, and that the Petitioner should not be heard to deny it—especially since the Claimant, *in reliance upon that agreement*, has changed its position and remitted its

money to K. N. & K. In such circumstances, we respectfully submit that the agreement should be construed to mean what it says unless the *Petitioner* convinces the Court, without "vagueness or uncertainty," that it could not reasonably have been so understood by the Claimant.

There is no dispute that the Claimant sent its remittance to K. N. & K. for the purpose of providing a fund for the payment of a draft which Claimant had drawn, in reliance upon the terms of the Drawing Service, which provides that K. N. & K. are to be "*employed*" as Claimant's "*agents*" for the specified purpose

> "of advising the issue of their drafts and providing the drawee banks with sufficient funds to cover their payment"

Neither can it be denied that in the Book of Foreign Drafts prepared by K. N. & K. and supplied to the Claimant they printed a stub which was to be the "Issuing Bank's Record" after it should have detached the Draft and the Advice, and that on this "Issuing Bank's Record" K. N. & K. had printed (fols. 479-480):

> "Paid K. N. & K _____
> (*transfer agents*)
> Profit $ _____ "

The Petitioner contends that in spite of its terms, the use of the Drawing Service by an inland bank created no agency. This result is claimed to follow from eight circumstances (pages 59-64), which we shall discuss briefly, giving to each of them the number which the Trustee has assigned to it.

> 1. The terms of the "Introductory Statement" in the list of Foreign Correspondents (Brief, pages 59-60).

The Trustee argues that this statement furnishes some evidence of an independent contractor relationship, because it states that upon the receipt of the proper advices and New York funds,

> "K. N. & K.'s advices are sent abroad and 'sufficient' funds for the payment of the draft provided to the drawee bank 'by transfer of credit from our balance or otherwise' " (brief, page 60).

The Trustee lays particular emphasis upon the use of the word "sufficient." Whether that word, if contained in the "Introductory Statement," would have improved the Trustee's position, need not be argued because the word "sufficient" is not there. The statement reads (fols. 419-420):

> "Upon receipt of proper advices, and New York funds to cover such drafts at the rates quoted by us for the day on which the drafts are sold, *our advices are at once forwarded and funds provided with the respective drawee banks for the payment thereof*, by transfer of credit from our balance or **otherwise.**"

The word "sufficient" is conspicuous by its absence.

The fact that the bankrupts reserved the right to provide the fund abroad "by transfers of credit from our balance or otherwise," is not inconsistent with the theory of a trust. The New York Court of Appeals made this clear when it said, in the *Legniti* case (230 N. Y., at p. 421), that where a customer gives moneys to a banker for remittance abroad and a trust arises

> "It is the amount which he gives that is to be transmitted. *How* it is sent may be immaterial to

> him. If there be time, currency might be purchased and sent. If not, *it may be transmitted in any form recognized in financial circles.*"

The Claimant supplied the "amount" to be transmitted. *How* it would be transmitted was "immaterial." "Any form recognized in financial circles" would suffice. Hence the mere fact that the bankrupts were left to choose their own method of transmission does not negative the trust relationship.

> 2, 4 AND 5. THE USE OF THE WORDS "SUFFICIENT FUNDS" IN SUBDIVISION 1 OF THE "TERMS AND CONDITIONS GOVERNING THE USE OF K. N. & K. DRAWING SERVICE" AND K. N. & K.'S FREEDOM OF METHOD OF EFFECTING TRANSMISSION (BRIEF, PAGES 60, 61, 62).

Much stress is laid upon the fact that the bankrupts undertook only to provide the foreign bank with "sufficient funds" for the payment of the draft, and it is argued that the use of these words indicates that it was not intended that the very money which the Claimant sent to the bankrupts was to be sent abroad by them.

We have already shown that in the "Introductory Statement" which admittedly "explains the underlying purpose of the service" (Petitioner's Brief, p. 59) the word "sufficient" does not appear. It would, however, make slight difference, even if it did appear in the "Introductory Statement," as well as in paragraph 1 of the "Terms and Conditions." The meaning of the word "sufficient" is clear from a consideration of the plan of the service. The bankrupts issued a rate card each day upon which they stated the rate at which remittances should be made to them "to cover" drafts drawn that

day. This rate included not only a sum equal to the foreign exchange value of the draft on that day, *but in addition thereto, an amount fixed by K. N. & K. to compensate them for their services in the matter* (fol. 70). How much represented one and how much the other, was not stated on the rate card (fol. 483). Out of the moneys remitted to them, K. N. & K. were to forward only that portion which was required "to cover" the draft. The balance they were to retain for their compensation. After having provided for the remittance to them of "adequate funds," K. N. & K. could not agree to provide the foreign bank with the exact amount so received because "adequate funds" included not only "sufficient funds" to cover payment of the draft drawn, but K. N. & K.'s compensation in addition. The word "sufficient" is used simply to define, without disclosing it, the portion of the total amount remitted to K. N. & K. by the inland bank which was to be applied by K. N. & K. to the payment of the draft advised.

The Petitioner argues (page 61) that the word "sufficient" is inconsistent with the Claimant's theory that there was an obligation assumed by K. N. & K.

> "to 'forward' or to 'remit' *the* fund or moneys which they received from Trinidad. *They could provide any funds to the foreign bank at any time, and by any means as long as they were sufficient to cause the draft to be 'protected' upon presentation.*" (Italics Petitioner's.)

The Claimant has never contended that K. N. & K. were required to remit the particular moneys received from Claimant and no such intention is necessary to the creation of a trust. Latitude in the choice of the means

to be employed in carrying out the purpose of the remittance would not have affected the relationship. In the *Legniti* case (230 N. Y., 415) the Court described the usual methods employed by financial institutions in selling credit, "usually represented by draft or check" and determined that the money paid therefor to the institution becomes the latter's property and does not establish a trust relationship. Judge Crane then goes on to say (pages 420-421)

> "There is a marked distinction between these transactions which I have just described and a direction to a bank or other person to transmit a certain specific sum of money to a person abroad. In such cases the Bank or transmitter is the agent of the person paying the money, and until the money is sent, holds it as agent or trustee for the owner * * *. In these latter transactions, the intention of the payer is that the money he gives to his agent shall be sent abroad. It is the *amount* which he gives that is to be transmitted. *How it is sent may be immaterial to him.* If there be time, currency might be purchased and sent. If not, *it may be transmitted in any form recognized in financial circles.* It is not at all necessary that the sender or agent have credit in the place to which the money is to be sent."

The Claimant here was interested in creating a fund of 24,360 Lira in the hands of B. C. I., for the payment of Draft No. 61161, which it had drawn. K. N. & K., for a consideration, offered, as Employees and Agents of the Claimant, and upon receipt of sufficient funds "to cover," to "provide" the drawee bank with that fund. The Claimant sent K. N. & K. "funds to cover," in accordance with the amount computed by the bankrupts. It was

interested in the transmission of this "amount." *How* the bankrupts sent it was "immaterial" to the Claimant. To paraphrase the words of Judge Crane in the *Legniti* case

> "It was 24,360 Lira which the Claimant wanted to have transmitted. If there were time, Lira might have been purchased and sent. If not, it might have been transmitted in any form recognized in financial circles."

The Federal Court in the Southern District of New York has followed the *Legniti* case and has held that a case like the one at bar falls within the hypothetical case described by Judge Crane in the *Legniti* case as a

> "Direction of a bank or other person to transmit a certain specific sum of money to a person abroad."
>
> *Matter of Pacat Finance Corporation*, 295 Fed., 394, 401.

In that case the Federal Trust Company of Newark, acting for Morris Shulman, sent its draft for $300 to the bankrupt, enclosing a letter which stated that the remittance was made "to cable *the equivalent* in Polish marks" to a named payee in Warsaw. As to this transaction, the learned Special Master (Now Mr. Justice Proskauer) held

> "First, the language of the letter of December 24, 1920, is sufficiently analogous with the hypothetical case described by Judge Crane in the *Legniti* case as a 'direction to a bank or other person to transmit a certain specific sum of money to a person abroad' " (citing several cases).

The findings and conclusions of the Special Master were confirmed (page 411). The letter referred to clearly showed that it was not intended or expected that the bankrupts would "forward or remit *the* fund or moneys" which it received from the Claimant there. It was to cable merely the "equivalent" in the foreign currency, just as K. N. & K. were to do here. Yet the Court held that the money was received with a

> "Direction • • • to transmit a certain specific sum of money to a person abroad"

within the meaning of that language as used in the *Legniti* case. In the case at bar, the money was sent to K. N. & K. upon their agreement "at once" and as "Agent" of the Claimant, to provide the drawee bank with the funds to cover the payment of the draft. K. N. & K. might have purchased and sent Lira, thereby forwarding "the equivalent" referred to in the *Pacat* case or they might have "transmitted it in any form recognized in financial circles," as stated in the *Legniti* case. The mere fact that they were not to "forward or to remit *the* fund or moneys which they received from Trinidad" would not render them any the less the agents and the fiduciaries of the Claimant.

### 3. The use of the word "protect" same upon presentation" (Brief, pages 60-61).

The Petitioner points out (Brief, page 60) that the "Advice" must be read "in conjunction with the 'Terms and Conditions' as it forms a part of the drawing service" and then proceeds to construe the Advice in *conflict* with the terms of the drawing service.

The Advice contained the direction to K. N. & K. "to protect" the draft. The Trustee argues that the use of

the word "protect" in the Advice shows that there was intended merely

> "A personal general obligation to see that the draft is paid." (Brief, page 61.)

In support of this construction, the Petitioner refers to definitions of the word "protect" given in dictionaries and in cases where the word was used in a context or under circumstances entirely different from those of the case at bar. In short, although the Petitioner starts out by urging that the Advice must be read in "*conjunction* with the Terms and Conditions" it seeks to have the Advice construed in *disregard* of the "Terms and Conditions." It disregards the fact that the word "protect" in the Advice is but a synonym for the *modus operandi* stated in the drawing service; that the drawing service provides (fols. 419, 420) for the transmission to K. N. & K. of adequate funds "to cover" drafts drawn by Claimant in its own name and contains the undertaking of K. N. & K. (fols. 423, 474, 475), "as the Agents of the drawers," upon receipt of said funds, to provide the drawee banks with sufficient funds "to cover" the payment of said drafts (fols. 420, 423); in short, that K. N. & K. would convert the American money given to it into a fund of Italian money with which to pay the draft and provide the foreign bank therewith. It is respectfully submitted that the citation of definitions of the word "protect" when used under circumstances and in a context entirely different from those present here, is not likely to be of service in arriving at the true construction to be given to the word "protect" as used in the Advice in this case (*Equitable Trust* v. *Rochling, supra*).

The Petitioner argues in this connection (p. 61) that the bankrupts were "simply paid in advance for their own general obligation to see to it that the draft drawn by Trinidad Bank was paid *at presentation*," (italics by Petitioner) because, it contends, the only obligation assumed by the bankrupts was that sufficient funds to pay the draft would be in the hands of B. C. I. *by the time the draft would be presented*. This construction does violence to the precise terms of the drawing service, which provides, *not* that the bankrupts should cause the necessary balance to be in the hands of B. C. I., *by the time the draft should be presented*, but that upon the receipt of the advice of the drawing of the draft

> "Our advices are *at once* forwarded and funds provided with the respective drawee banks for the payment thereof" (fol. 420).

and which also provides (fol. 422) that upon receipt of the advice

> "We shall *promptly* forward our advice of the same and provide the drawee banks with funds sufficient for the payment of the draft abroad."

K. N. & K. recognized this obligation. Our advice to them of the drawing of the draft was sent May 19, 1923 (fols. 481-483). On May 22, 1923, they forwarded their advice to B. C. I. and B. C. I.'s statement of account shows that on June 4th, 1923, K. N. & K.'s account was debited with the amount of the draft and "Drafts Payable" was credited therewith (fols. 508-510).

K. N. & K. did *not* merely undertake that by the time the draft would be presented they would have a sufficient *credit* there. Their credit was not involved. The drafts

were neither *drawn* by them nor *payable* by them and the holder of the draft would have no claim against them nor recourse to any balance in their favor.

6. The contention that K. N. & K. followed the same procedure with respect to drafts drawn by them as they did with respect to drafts drawn by inland banks under the drawing service (Brief, pages 62-63).

This claim is based on two circumstances. First, that K. N. & K., in the drawing service, refer in the same sentence to the rates at which they were prepared to "sell," and to the rates at which they were prepared to "provide for the payment," of drafts, and, second, the statement in the drawing service that where an inland bank desires to sell a draft on a place not mentioned in the list of foreign correspondents, the inland bank should buy a draft of K. N. & K. and not draw a draft in its own name.

We are unable to see in what respect either of these provisions of the drawing service tends to show that the drawing of a draft under the drawing service made K. N. & K. independent contractors rather than agents of the drawer. The rate upon which a draft would be sold was fixed by K. N. & K. upon the same basis as the rate upon which it would agree to provide for the payment of drafts drawn under the terms of the drawing service, to wit, the market price of the foreign currency involved. In these circumstances, it is only natural that the general provisions dealing with "rates" should be made to apply to both classes of transactions. *On the other hand, the very fact that K. N. & K. made separate provisions for the two classes of transactions indicates that, even in their minds,*

*they were of a separate nature and a provision with respect to one would not be deemed to include the other.*

7. THE STATEMENT IN THE DRAWING SERVICE THAT IF THE REMITTANCE BE MADE AT A WRONG RATE, THE BANKRUPTS MAY RETURN THE SAME OR ADVISE THE DRAFT ABROAD AND CALL FOR PAYMENT OF ANY DEFICIENCY (BRIEF, PAGE 63).

It is claimed by the Petitioner that the reservation of this right by K. N. & K. shows that they intended not to transfer "a fund," but to employ their "own credit." As we read this provision, it means merely that K. N. & K. reserved the right, *in cases where it felt that the credit risk was satisfactory*, to supply any deficiency in the remittance of an inland bank for the purpose of advising the draft abroad, and to rely upon the credit of the inland bank to make up the deficiency upon request. What the relation of K. N. & K. to the inland bank would be with respect to the amount supplied by them need not be considered, because the question is not here.

8. THE INCLUSION IN THE ADVICE TO THE FOREIGN BANK OF K. N. & K.'S OWN DRAFTS, AS WELL AS THE DRAFTS OF INLAND BANKS (BRIEF, PAGES 63-64).

It is urged that the Claimant's contention that there was an agency and a trust is negatived by the fact that in the steamer block, by which the foreign bank was advised of the drawing of the Claimant's draft, K. N. & K. also included drafts drawn directly by K. N. & K. and that the steamer block did not include directions to establish a credit for the Claimant; that it directed merely the honoring of the draft and the charging thereof to the ac-

count of K. N. & K. The Trustee argues that the transaction was the "usual, everyday banking transaction," where the American banker advises his correspondent to honor a draft drawn by the American banker and that

> "The situation only differs from the ordinary one in that K. N. & K., in addition to protecting its own drafts, assumed an obligation to protect in a similar way, the drafts of other drawer banks."

In other words, the contention is that because K. N. & K., in its advices to the B. C. I., listed the drafts drawn by it on the same advice on which it listed the drafts drawn by Claimant, the Claimant's contention that its money was remitted for a particular purpose is "negatived." To state this proposition is to refute it. How anything which K. N. & K. did in their private communications with B. C. I. (of which the Claimant had neither knowledge nor notice) can affect the relations of the bankrupts to the Claimant under the drawing service, is beyond our understanding. Whether K. N. & K. became the agents and the trustees of the Claimant depends upon the terms and conditions of the drawing service. Whatever the relationship was, it could not be affected, to the prejudice of the Claimant, by the private communications between the bankrupts and B. C. I. Certain it is that K. N. & K. could not diminish or destroy Claimant's rights by any liberties they took with their own. Furthermore, the mere fact that the bankrupts went through the same forms of procedure with respect to drafts drawn under the drawing service as they did with their own drafts, is no evidence that their obligations under these two classes of instruments were the same. The Court of Appeals in the *Leguti* case discussed the machinery employed in

making transfers of credit by cable or otherwise, and those employed in remitting a particular fund, and said (page 421)

> "The actual thing that is done by the sender in both of these cases may or may not be the same, but the practice of the merchants and banks has recognized a difference; so have the Courts."

We have now discussed the eight circumstances upon which the Petitioner relies in support of its claim that the evidence favors an independent contractor, rather than an agency, relationship, and we have shown that these circumstances do not support his conclusion; that on the contrary, they are all perfectly consistent with, and in fact support, the relation of principal and agent, which is the relationship expressly provided for in the agreement. Although, as we have shown, there is no merit to the Petitioner's contention that the bankrupts were independent contractors rather than agents, we cannot refrain, before leaving the subject, from asking: What difference would it make if K. N. & K. were independent contractors and not agents? There are some cases in which the distinction would make a difference, to wit, cases in which one is sought to be charged for the acts of another on the theory of *respondiat superior*. We submit, however, that in the circumstances of this case it would make no difference at all. According to the Petitioner, if K. N. & K. were independent contractors they would have had a greater latitude in selecting the means for performing their "function" than if they had been agents. What of it? Latitude in that respect would not affect the result in this case. (*Legnitz* v. *Bank*, *supra*). Whether they were "independent contractors" or

"agents" or just plain "servants," the fact would still remain that the Claimant delivered money to them for a particular purpose and that unless they applied the money to that purpose, they must return it.

The Petitioner's next contention is (Brief, page 64), that the use of the words "principal" and "agent" are not controlling and do not negative the conclusion that the parties dealt as independent contractors.

We are free to admit that the use of the words "principal" and "agent" are not controlling; that the mere use of these words would not create that relationship in a case where, *from the circumstances, it was clear that no agency was intended.* There is, however, nothing in the facts and circumstances of this case which show that no agency was intended. On the contrary, they show that an agency *was* intended. The Claimant had drawn a draft payable abroad and was under the necessity of providing the drawee with a fund with which to pay it. It had received from K. N. & K. their offer, contained in their drawing service, to become

> "Employed merely as the agents of the drawer for the purpose of advising the issue of their drafts and providing the drawee banks with sufficient funds to cover their payment" (fol. 423)

and had also been advised by K. N. & K. that under the arrangement which they proposed, the Claimant would draw its own drafts as PRINCIPAL and, as far as K. N. & K. were concerned, their

> "Sole function (would be) to advise the drawees of the issue of drafts drawn by our correspondents and to provide for payment, *in which function we act as agents of the drawees.*"

The Claimant, in reliance upon this offer, remitted its money to K. N. & K. It cannot be said that the circumstances of the case make the use of the word "Agency" a misnomer or that no agency could have been contemplated in the transaction. An agency *was* within the purview of the transaction and K. N. & K. agreed to act as such in it. As we stated previously, the Claimant should not now be prejudiced by a construction of the contract which will give the words used by K. N. & K. a meaning different from what they expressly say, *unless the Petitioner shows, without vagueness or uncertainty, that the Claimant could not reasonably have understood the words to mean what they say.* This the Petitioner has failed to do. K. N. & K.'s offer to act as agent is clear, unambiguous and in language chosen by them. An agency was certainly within the purview of the transaction and is expressly provided for—indeed, *emphasized*. The agreement is reasonably susceptible of the construction placed upon it by Claimant, and in reliance upon which it parted with its money, and the Petitioner should not be heard to dispute it.

In its brief in the Court below the Petitioner contended that the term "Agent" was used in the Drawing Service in "the loose or lay sense" and merely as the "correlative" of the word "Principal," which was used shortly before it. This claim was baseless and appears now to be abandoned. The word "Principal" was used to define the relation *between the Trinidad Bank and its customer*. The Drawing Service points out that the inland banks "act as PRINCIPALS, and issue drafts in their own name, our (K. N. & K.'s) name not appearing thereon." This is entirely consistent with the subsequent use of the word "agent" *in defining the relation between K. N. & K. and the inland banks*. The purpose is to im-

press the fact that the inland bank does not issue K. N. & K. drafts as an agent of K. N. & K.; that it issues its *own* drafts as PRINCIPAL, and is *in fact* the PRINCIPAL, both in its relations with its customer *and* with K. N. & K.—K. N. & K. acting as *its agent* and *employee* for a limited specified purpose. This also makes it clear that *K. N. & K. assumes no responsibility beyond the use of reasonable diligence to carry out the inland bank's instructions.* The words are clear, both in the Terms and Conditions (fol. 423) and in the book of foreign drafts (fols. 474-475). The Bankrupts are "*employed* merely as the *agents* of the drawers" (fol. 423) and their "sole function" is to advise the Drawee of the issue of drafts and to provide for payment "in which function we act as agents of the drawers" (fol. 474). How could one's intent to limit his responsibility to that of a mere conduit be more perfectly expressed? There is nothing in this clear and unequivocal language, selected by K. N. & K., to justify the argument now made by the Petitioner in its attempt to avoid the agreement upon which this Claimant relied. The claim that K. N. & K. used the word "agent" in a "loose or lay" sense, cannot improve the Petitioner's position to the prejudice of the Claimant. The Drawing Service was a matter of great importance to K. N. & K. The language in it was, no doubt, chosen by representatives specially selected by them for the purpose and with the deliberation which the importance of the subject required. The Petitioner cannot avoid its effect on the ground that the draftsman was "loose" in his choice of words.

Nor is it an answer to the Claimant's contention to say that some other construction is *possible*. The language was chosen by the Bankrupts. If it is equivocal or

indefinite, the fault is theirs and all doubts must be resolved against them. The only question is: Is the language of the Drawing Service reasonably susceptible of the construction which the Claimant placed upon it and in reliance upon which it remitted its money to K. N. & K. If it is, that construction is binding upon K. N. & K. and their Trustee.

Under the title "No Technical Agency," the Petitioner argues (Brief, pages 68-71), that there are three tests to be applied in determining whether an agency was effected,

(a) Control of the means of performance.

(b) Bringing the principal into contractual relations with third parties.

(c) The assumption of risk of profit and loss, and that the Claimant has not met these tests.

(a) The Court of Appeals of the State of New York has decided that the control of the means of performance is *not* necessary to the establishment of a trust.

> *Legnati* v. *Mechanics & Metals National Bank*, 230 N. Y., 415.

In that case, as we have already pointed out, the Court distinguished between "sale of credit" cases and "transmission" cases and stated that in the latter cases (p. 421):

> "It is the *amount* which he gives that is to be transmitted. *How it is sent may be immaterial to him. If there be time, currency might be purchased and sent. If not, it may be transmitted in any form recognized in financial circles.*"

See also 2 C. J., 423, where the learned author of the Article on "Agency" says

> "The agent is to accomplish a certain end, *in general using his own discretion as to the means adopted.*"

The answer to the Petitioner's claim that the Claimant has not met the test of "Control of the means of performance," is that there is no such test.

(b) The second test which it claims has not been met, is "Bringing the principal into contractual relations with the third party." In discussing this alleged test, the Petitioner begs the question. The Trustee *asserts* (p. 70) that the bankrupts were not employed to set up a credit with the B. C. I., and that B. C. I. assumed no obligation to Trinidad; that it had no account on its books in favor of Trinidad and that its contractual relations remained solely with the bankrupts. There is no evidence in the record to support these statements. The Trustee refers to folio 419 as his authority for them but nothing in that portion of the record supports them. The thing for which K. N. & K. was employed, according to their own statement (fol. 423), was

> "as the agents of the drawers for the purpose of advising the issue of their drafts and providing the drawee banks with sufficient funds to cover their payment"

and (fols. 474-475) to advise the drawee of the issue of drafts

> "and to provide for payment, in which function we act as agents of the drawers."

These provisions, read in the light of the scheme of the drawing service, and the acts performed thereunder, show that the bankrupts not only were "employed" to, but, actually *did*, bring their principal "into contractual relations with third parties." The Bankrupts were "Employed" as Claimant's "Agents" to cause a fund to be created in the hands of B. C. I. for the payment of drafts drawn by Claimant. Claimant gave them the money with which to do it, and in addition a sum to compensate them for their services. *They actually caused B. C. I. to create that fund*, which it did by taking the necessary moneys out of K. N. & K.'s credit balance and crediting it to a separate account, entitled "Drafts Payable." This account was kept by B. C. I. (fol. 356) to enable it to be in a position to meet *its* "commitments." This "commitment," it will be observed, is not a commitment from B. C. I. to K. N. & K. It is a commitment to a stranger —an obligation to the holder of the draft which the claimant had drawn—an obligation assumed *for the benefit of the claimant* because the claimant, as drawer of the draft, was obligated to see it paid. In view of these circumstances, it is difficult to understand on what theory it can be claimed that K. N. & K. did not bring the inland bank into contractual relations with B. C. I.

The statement on page 70 of the Petitioner's Brief, that B. C. I's contractual relations remained solely with K. N. & K.

> "to whose account it was directed to debit the draft upon its presentation"

is a misstatement which, while no doubt inadvertant, is misleading. There is no evidence that K. N. & K.'s account was not to be debited with the amount of the draft

advised until its *presentation*. The undisputed evidence is to the contrary and shows that the account of K. N. & K. was intended to be and actually was debited *immediately* upon the receipt by B. C. I. of K. N. & K.'s advice that the draft had been drawn; that thereupon the necessary amount was immediately transferred to the Drafts Payable account, kept by B. C. I. as a record of its own obligations (fol. 356). Immediately upon the happening of this event K. N. & K.'s responsibility to Claimant ceased and a contractual relation between B. C. I. and the holder of the draft and Claimant, who had drawn the draft and was liable for payment thereof, was created. This met the second alleged test of

> "Bringing the principal into contractual relations with the third parties."

(c) The third test in determining the existence of an agency relation is claimed (Brief, pages 70-71) to be

> "Whether the alleged principal or agent bears the risk of profit or loss in the transaction."

It is claimed that if the agent bears the risk he is

> "an entrepreneur and is an independent contractor and not an agent."

The Petitioner claims, with the courage which comes after the event, that the risk of loss from the decrease in the value of the Lira prior to the presentment of the draft was on the Bankrupts and that it follows from this that they

> "must have acted as principals and independent contractors."

This argument is founded on premises not only unsupported by the record, but *contrary* to the record. The principal fallacy lies in the assumption that K. N. & K. was permitted to speculate upon the rise and fall of foreign currency between the time of its receipt of the advice from the inland bank and the time of the presentation of the draft. *It was not contemplated that the Bankrupts should have the right to wait until the draft was about to be presented to create the fund abroad. If they did so, they acted in violation of the terms of the Drawing Service.* In the Introductory Statement of the Drawing Service (fol. 420), K. N. & K. undertake that upon receipt of proper advices and adequate funds to cover at the rates quoted by them for the day on which the drafts are sold by the inland bank

> "Our advices are *at once* forwarded and funds provided with the respective drawee banks for the payment thereof."

Again, in paragraph 1 of the Terms and Conditions, K. N. & K. undertake that upon receipt of advice of the drawing of the drafts and adequate funds (fol. 422)

> "we shall *promptly* forward our advice of the same and provide the drawee with funds sufficient for the payment of the drafts abroad."

Still again, in the book of foreign drafts, the Bankrupts undertake that upon the receipt of the advice of the drawing of the draft and adequate funds (fol. 474)

> "we shall *promptly* forward our advice of same and make provisions for its payment abroad."

*Not only was this K. N. & K.'s obligation, but the uncontradicted evidence is that they performed it, by set-*

*ting up the fund immediately upon receipt of claimant's advice* (fols. 481-483, 487). *In other words, K. N. & K. never questioned their obligation to set up the fund as soon as they received notice of the drawing of the draft and funds to cover; it has remained for the Petitioner to assert such a claim.*

K. N. & K. fixed the amount which was to be remitted to them upon the basis of the market on the day the draft was drawn. If they carried out their agreement to create the fund "at once" and "promptly" upon receipt of the advice and funds, there would be no opportunity for loss or gain by reason of fluctuation in the market. The only way fluctuation could effect them would be if, instead of creating the fund abroad "at once" or "promptly," they waited until at or about the time they estimated the draft would be likely to be presented and speculated upon the drop in the price of the foreign currency in the interim. If they had done that they would have violated the terms of the drawing service.

K. N. & K. were carrying on "a foreign exchange business" (fol. 419). As the Petitioner admits (Brief, p. 3) they were large dealers in foreign exchange and maintained large foreign balances. There is nothing in the drawing service to indicate that they did not intend to do busness with the inland bank on the basis of currency *actually in hand*. As to any such foreign currency, K. N. & K. knew exactly what it had cost them and upon what basis they could afford to assign portions of it to the payment of drafts drawn under the service. Such transactions were not subject to any risk "of profit or loss in the transaction." They reserved the right to provide the fund abroad "by transfers of credit from our balance or otherwise" (fol. 420). This, however, does

not suggest that they intended speculating against the market between the time of their receipt of the inland bank's advice and the time when they estimated the draft would be presented abroad—and the evidence shows that they did not. The "otherwise" was apparently inserted merely to save K. N. & K. from being tied down to any one specific method of transfer.

The third alleged test of "the assumption of risk of profit or loss," must be resolved in favor of the Claimant, because the plan of the drawing service permitted of no "risk of profit or loss" on the part of K. N. & K.—their profit being only the amount which they included in the rate card to cover their compensation, and this was not subject to risk of rise or fall.

**THE ADJUDICATED CASES ESTABLISH THAT K. N. & K. RECEIVED THE CLAIMANT'S MONEY IN TRUST FOR A PARTICULAR PURPOSE.**

The rule has long been established in England that sums of money delivered to a bank for the payment of an obligation of the payor at some other place is money held by the bank in trust for a specific purpose and if not so applied belongs to the payor. The leading English case is *Farley* v. *Turner*, 26 L. J. Ch., 710. It has been frequently cited and followed in the American decisions. In this case one Goodwin having accepted a bill, payable at Robarts & Co., paid into the hands of his bankers, Messrs. Farley, Turner & Jones, the sum of £707. He told the bankers' clerk that £500 of this money was to be used to meet said acceptance on December 14th, and he notified Farley, Turner & Jones in writing to advise Robarts to pay the same. The bankers thereupon sent to Overend & Gurney certain bills to discount and directed them to pay the proceeds to Robarts for the pur-

pose of meeting Goodwin's acceptance, as well as others. This was done on the 11th of December and on the morning of the 12th Robarts received information that Mr. Turner of the firm of Farley, Turner & Jones, had died the preceding evening and the firm had ceased to carry on business. The £500 was not applied in payment of Mr. Goodwin's acceptance but was subsequently paid over to the representative of Mr. Turner's estate. Vice-Chancellor Kindersely held

> "that the £500 belongs specifically to Goodwin and not to the general creditors of Mr. Turner."

In the course of his opinion he said (p. 711):

> "According to the statement in the case, it appears that at the time of paying in the £707 Goodwin told the clerk that £500 of this money was to be applied for the specific purpose of meeting an acceptance, payable at Robarts & Co.'s, to become due on the 14th. Goodwin at the same time signed the notice before stated. Now, what was the effect of this direction to the bankers? Goodwin in effect said, 'There is a bill which I want paid at Robarts & Co., therefore send them £500 of this money and advise them to apply it in payment of this bill.' The direction is accepted by the bankers, or by their clerk, which amounts to the same thing, and the clerk did what appears to be usual. There was no negligence on his part; at the same time he placed the whole amount of £707 to Mr. Goodwin's general banking account. He might certainly have sent up a cheque for £500 to Messrs. Robarts & Co., and placed the remaining sum to Mr. Goodwin's account, but he took the ordinary course and sent up the £500, debiting Mr. Goodwin's banking account with that sum, and they informed Robarts & Co. that such a bill would be presented. Now, it so happened that the Kidder-

minster Bank had other bills, more or less under similar circumstances, which they wanted paid at Robarts' bank, and they sent up a batch of bills to Messrs. Overend & Gurney for them to discount, and directed them to pay the amount into Robarts & Co.'s bank for the purpose of meeting other bills, as well as that for £500. It appears to me that the course pursued was the same as if, having no occasion to pay more than the £500 bill, they had simply sent up the specified amount with a direction to pay that particular bill. *It is true that the money was not earmarked as if it had been locked up in a box, but it is a portion of the £707 which had been paid in expressly for the purpose of meeting the bill for £500.* The facts of this case differ, I think, from the cases cited. I admit that the money is not a particular deposit with the bankers, but *it is money placed in their hands to be applied in a particular way.* What I now decide will not trench upon the authorities which decide that money paid into a banker's is not a deposit which you may receive back in the identical notes and sovereigns, but that it is a debt. *That is quite a different case.*"

See also, *Giles* v. *Perkins*, 9 East., 12, and *Burdett* v. *Willett*, 2 Vernon, 638.

The American rule, both State and Federal, follows closely the law of England and is stated in the following cases:

*In re Jarmulowsky*, 258 Fed. Rep., 231;
*In re A. Bolognesi & Co.*, 254 Fed. Rep., 770;
*City of St. Louis* v. *Johnson*, 5 Dillon, 241;
*Massey* v. *Fisher*, 62 Fed. Rep., 958;
*Moorehead* v. *Brown*, 86 Fed. Rep., 257;
*People* v. *City Bank of Rochester*, 96 N. Y., 32;
*Cutler* v. *American Exchange Natl. Bank*, 113 N. Y., 593;

*People ex rel. Zotti* v. *Flynn*, 135 App. Div., 276;
*Peak* v. *Ellicott*, 30 Kansas, 156, 1 Pac., 499;
*Ryan* v. *Phillips*, 3 Kans. App., 704; 44 Pac. Rep., 909;
*Star Cutter Co.* v. *Smith*, 37 Ill. App., 212;
*Roca* v. *Byrne*, 145 N. Y. 182.

In the *Jarmulowsky* case (258 Fed. 231), the bankrupts were private bankers until they suspended business and passed into the hands of the State Superintendent of Banking. The petitioner paid to them the sum of $288, receiving therefor a receipt which set forth that the money was to be forwarded to a definite person at a specified place in Europe "subject to conditions" on the back of said receipt. Of these conditions the first was "*it is previously understood that we act as agents only for the sender.*" The bankrupts never forwarded the money, were admittedly in possession of the same on the day of the failure, and it passed to the trustee in bankruptcy. Upon an application for the repayment of this money the Court (Ward, Rogers and Hough, Circuit Judges), held that the claimant could recover funds which he could trace and identify and that this right was superior to the right given a depositor under section 156 of the Banking Act of the State of New York upon the insolvency of a private banker. The Court said:

> "That the Jarmulowskys in receiving this money acted in a fiduciary capacity, and that the person intrusting such money to them may on tracing the same into the possession of the trustee in bankruptcy recover it in solido, is sufficiently

shown by our recent decision in *Re Bolognesi* (254 Fed., 770). * * *

The statute was not intended to do and does not take away from persons dealing with a private banker as 'depositors' or 'transmitters' any rights or privileges, legal or equitable, which by general law they possessed prior to the passage of said act. It does exclude all creditors from participation in certain specified assets, until the claims of depositors and transmitters are satisfied.

The granting of such priority or preference is by statute made a condition for the lawful transaction of the business of private banking; but such preference cannot of itself deprive a man of the right of tracing and claiming *his own money* when found in the possession of an unfaithful fiduciary —which is all that has occurred in the present instance. * * *

In so far as the trustee represents such preferred creditors, he is benefited by the order complained of; in so far as he represents general creditors, neither they nor he, as their representative, have any right to keep funds which are identified as the very money of petitioner below."

*In Re Bolognesi & Co.* (254 Fed., 770), distinguishes between the deposit of funds with a banker for use in a specified manner and the purchase of drafts and money orders. As to the first class, the Court said:

"In so far as any claimant gave money to the bankrupt for investment in a specified manner, the bankrupt undoubtedly, by accepting the deposit, undertook to act in the interest of the depositor claimant, and thereby assumed toward him a fiduciary relation. (*Johnson* v. *Brooks*, 93 N. Y., at page 342); and in so far as such claimants traced their funds into the Central Trust Company account they stand in the position recognized and enforced in *re Hallett*, 13 Ch. D., 696, followed

in *National Bank* v. *Insurance Co.*, 104 U. S., at page 68, 26 L. Ed., 693. It follows, under the findings, that the Scranton Trust Company, Lagnese (to the admitted extent of $1,687.06), Gualtiere, Verrili, and Rescigno (to the extent of $550.70), were *prima facie* entitled to share in the fund, because Bolognesi had not fulfilled his duty as a fiduciary in respect of them."

*City of St. Louis* v. *Johnson* (5 Dillon, 241). The City of St. Louis kept two accounts in the National Bank of the State of Missouri (which suspended payment and went into liquidation on June 19th, 1887). From these accounts the City drew moneys from time to time to provide funds for bonds and coupons of the City falling due and payable in the City of New York. It was the custom of the City Treasurer to draw a check on the National Bank of the State of Missouri for the amount necessary to be placed in the New York bank to pay maturing bonds and coupons, endorse the check and deliver it to the bank with written instructions to remit the amount to the National Bank of the Republic or the National Bank of Commerce in the City of New York to pay bonds and coupons of the City of St. Louis falling due. Thereupon the National Bank of the State of Missouri would remit or provide a credit for the amount specified to the New York Bank with written instructions to the said Bank to pay and charge to the general account of the National Bank of the State of Missouri the bonds and coupons of the City of St. Louis maturing at said Bank and to forward the same cancelled to the National Bank of the State of Missouri. The National Bank of the State of Missouri paid the City of St. Louis interest on its average daily balance in its current ac-

count but none on the sums remitted to New York after the bank received the check of the City Treasurer therefor. The Court said:

> "* * * The bank was the general debtor of the city, having funds subject to its check or draft. Let us take the transaction of April 25th, for it represents all the others. The city comptroller directs the city treasurer 'to remit' to the Bank of the Republic $51,000 to pay the bonds and coupons of the city falling due at that bank on the following month. On the same day the city treasurer draws in favor of the bank his check for the amount and encloses it to the president of the bank, with directions, *inter alia*, 'to remit' to the Bank of the Republic, in New York, $51,000, 'to pay bonds and coupons of the city falling due (at that bank) in May next.' The bank at once charges the amount of that check to the city, which has the effect to reduce the city's balance with the bank and to stop interest to that extent. If the money had been passed over the counter to the city treasurer, and he had delivered it to another bank, with instructions to remit to a particular bank for a specified and definite purpose, such bank would have been the agent of the city to remit or transmit the money of the city; it would remain the money of the city, notwithstanding it may have been credited on account to the agent, and not to the principal, and this with the consent of the two. If such bank had transmitted the money by express, the money would be the city's; if by draft, it would be the agent of the city for that purpose; but when its instructions were obeyed and the money duly received by the appointed depository, all liability would be at an end. If the appointed depository failed, the loss could not be thrown upon the agent.
>
> "But the money was not paid over the counter to the city, and the city did not select some other

agent or bank to remit or transmit it to the Bank of the Republic, but selected its general depository to make the remittance, and accepted a credit in another account for the same sum. The bank remitted the sum, as directed by the city, to the Bank of the Republic, with specific directions to credit the amount to it, and to use the same 'to pay the bonds and coupons of the city maturing at your bank next month', and charge the amount to the account of the bank here, and forward to this bank the bonds and coupons cancelled.

"The letter of the treasurer to the president of the bank made the bank here the agent of the city to remit, and if the bank here did remit accordingly, and placed the sum with the designated bank, i. e., the Bank of the Republic, it did its duty, and would not be liable to the city if the Bank of the Republic had failed with this fund on hand. * * *

"The bank charged the city with exchange on the amount it thus received, the same as it would have charged if the draft had been for any other customer. It became the agent of the city to transmit the money. The money, when placed in the Bank of the Republic, was, as between the Missouri bank and the city, the money of the latter. When the agent presented coupons cancelled, this showed that the agent had discharged the duty it had undertaken.

"It is my judgment that the relation between the Missouri bank and the city, as respects the money deposited with the Bank of the Republic, was not that of debtor and creditor strictly, but that of principal and agent, with the duties and liabilities of the latter, and not those of the former relation. The moneys deposited by the Missouri bank in its name with the Bank of the Republic, were, as between the former bank and the city, *trust moneys*, and in equity they belong to

the *cestui que trust*, and the latter has the right to pursue and claim them as against all persons who do not stand free of the trust."

The leading case in New York is *People* v. *The City Bank of Rochester*, 96 N. Y., 32. In that case the firm of Startwell, Hough & Ford of Rochester were depositors with the Rochester City Bank. The bank had from time to time discounted their notes payable in the city of New York but with the understanding that they should in fact be paid at the bank. In November, 1882, two of their notes, one for $3,000 and one for $5,000, were outstanding, and wishing to anticipate payment they gave the bank their check for the amount, less rebate of interest, of the $3,000 note. The bank charged the check to their account and at the same time made an entry in its books to the effect that the note was paid. Substantially the same transaction took place with reference to the second note of $5,000. The bank had previously sold both notes and received from the purchaser the proceeds thereof, but of this the firm was ignorant. About a month later the bank was declared insolvent and a petition was brought to compel the receiver to pay the note. The Court held:

"The transaction in question was not between the bank and Sartwell, Hough & Ford in their relation of debtor and creditor nor in their relation of bank and depositor. The object of the latter *was to provide a fund for the payment of specific notes, and the engagement of the former was to apply that fund to such payment. Thus a trust was created, the violation of which constituted a fraud by which the bank could not profit, and to the benefit of which the receiver is not entitled.* (*Libby* v. *Hopkins*, 104 U. S., 303; *In re Le Blanc*,

14 Hun, 8; affirmed 75 N. Y., 598). Those cases stand upon the ground of a specific appropriation of a particular fund for the payment of the claim there brought in question. So does the one at bar. * * *

"Counsel for the appellant contends 'That there never was any fund set apart for a particular object, or any intention or purpose to set apart such a fund.' I do not regard this, if true, as of much importance, but the appeal papers do not permit us to accept such construction.

"The checks of the petitioners were money assets in the hands of the bank and were so treated by all parties; they were delivered to it with explicit directions to apply the proceeds on payment of the notes; those directions were assented to by the bank officer, and the checks collected from the general fund. From that moment the bank was bound to hold the money for and apply it to that purpose, and no other, or failing to do so, return it to the petitioner. As to it, the bank was bailee or trustee, but never owner. It is estopped from saying that all this is matter of bookkeeping. It assumed a duty, and the receiver as its representative is bound by it. Nor does this obligation at all depend, as the appellant seems to suppose, upon the question, when, where, and to whom the notes were to be paid; whether presently or in the future is immaterial.

"*The specific object for which the fund was created was the payment of the notes, and its character does not depend upon those incidental circumstances. The checks were impressed with a trust, and no change of them into any other shape could divest it so as to give the bank or its receiver any different or more valid claim in respect to them than the bank had before the conversion.*"

In *Cutler, et al.* v. *American Exchange National Bank*, 113 N. Y., 593, the plaintiffs were depositors with the

defendant bank. Desiring to remit a sum of money to one Hall in Leadville, Colorado, they applied to the defendant to do it for them. The defendant refused to give a draft on a bank in Leadville but agreed to and did give plaintiffs a letter of advice for which plaintiffs paid $500. This letter of advice was addressed to the bank of Leadville, Leadville, Colorado, and stated in substance that their account was credited on that day with $500 received from the plaintiffs for the use of J. Seymour Hall and was signed by the defendant's cashier. The plaintiffs forwarded the letter, but before it was received the Leadville bank had failed and the receiver thereof refused to pay any money. Plaintiffs thereupon received back the letter and then demanded that the defendant carry out their undertaking to transmit the money to Hall or pay back the same to the plaintiffs. The Court said:

> "This appeal turns upon the understanding and agreement between these parties. That they made a distinct compact is not to be doubted, and the plaintiffs' construction of it seems to us as logical as it is natural. The agreement must control the respective rights and duties, and it is to be determined by what was said and done between the parties, when the plaintiffs paid their money to the defendant. *The plaintiffs wished to make a payment to a certain person, in a distant state, and the defendant undertook to effect it for them in its own way. When the plaintiffs assented and paid in the sum desired to be remitted, they received the paper writing in question. From that moment the defendant became a depositary of a fund, which was, by its own agreement, devoted to one particular purpose and to no other.* If that purpose failed, or became incapable of being effectuated, or was recalled by the plaintiffs, the

absolute right to the moneys was in them and in no one else.

* * * The plaintiffs paid the money to defendant as a conduit for its transmission to Hall, and its undertaking was that Hall should get it. The letter of advice, which plaintiffs received, by its terms, limited the use of the money to him alone. The defendant became the special depositary of the fund, and bound itself to retain it, until drawn out under the authority of the letter.

* * * Thus the meaning of the instrument was obvious to the plaintiffs, to Hall and to the foreign bank. It evidenced a special deposit made by plaintiffs, and warranted and protected the foreign bank in paying the sum mentioned to Hall upon its production and surrender. * * *

As there was an express contract made with plaintiffs by defendant to do the particular thing, the defendant must be bound by its terms and legal effect. As we have said, the compact was clear enough, and whatever forms the defendant went through, it would not be allowed to change it, or to divert the moneys to any other purpose or use.

* * * Here was an express agreement entered into between these parties for the accomplishment of a particular purpose, and to which the money paid to the defendant was dedicated from the moment of its receipt. * * *

* * * The deposit was a special one, for a designated beneficiary and could not be used or dedicated by the defendant to any other purpose. *No system of bookkeeping entries would be allowed to cause the plain agreement of the parties to miscarry; either with respect to a payment to Hall, or to its return to the depositors, in the event of the failure of the defendant to cause such payment.*"

In *Massey* v. *Fisher*, 62 Fed. 958, money was delivered to a bank for the purpose of taking up a note. The Court said:

> "The plaintiffs claim that the transaction established a fiduciary relation between the parties, while the defendant claims that it established the relation of debtor and creditor only. If the question was new, its proper solution might be open to doubt. Even in such case however, I would adopt the plaintiffs' view. The money was delivered and received to extinguish the note. *Neither party contemplated that the bank might use it for another purpose, leaving the note outstanding, and the plaintiffs' liability unextinguished.* Such application of it therefore, would be a violation of duty, and a fraud.
>
> "But the question is not new; it arose, and was decided, in *People* v. *City Bank of Rochester*, 96 N. Y. 32. The facts there were substantially like those before us. It is true the check in that case was drawn in terms, to pay the note. This, however, is an immaterial difference. It is as plain here as it was there that the money was delivered and received to take up the note. In *Peak* v. *Ellicott*, 30 Kan. 156 (1 Pac. 499), the facts were identical with those before us. In each of these cases it was held that the transaction established a fiduciary relation between the parties.
>
> "The bank having failed to apply the money to the note can it be recovered from the receiver? His counsel thinks not, because the bank placed the money in its vaults with other money of its own, whereby its identity was lost. Why should this wrongful act defeat the plaintiff's right? Nobody is injured by allowing the plaintiffs to take the amount from the deposit. The receiver and creditors stand on no higher plane than the bank, and can no more assert that it was the bank's

money than the bank could. It is true they are entitled to all the bank's property; but this was not its property. It is not important that the plaintiff's money bore no mark, and cannot be identified. It is sufficient to trace it into the bank's vaults, and find that a sum equal to it (and presumably representing it), continuously remained there until the receiver took it. The modern rules of equity require no more."

Justice Stone, in an article in the Columbia Law Review (21 Col. Law Rev. 510), written while he was Dean of the Columbia Law School, states the rule in ordinary course of business as follows:

"Since in the ordinary course of business, when money is paid over to B for transmission to C, B is not expected to turn the identical money over to C, and since the legal relationship in such transactions had been worked out by the law courts long before the establishment of equitable trusts of money, *such transactions presumptively give rise to the fiduciary relationship rather than to either a bailment or a trust.* Hence it is in Anglo-American law that we find a traditional judicial bias rooted in the history of the subject *in favor of holding the receiver of money for transmission to the duties and liabilities of fiduciary.*

• • • • • • •

"The notion that a person or corporation receiving money for account of another or as his agent to pay to another is a fiduciary, for reasons already referred to, was firmly engrafted on our law long before the development of banking business as it is carried on in modern practice."

Justice Stone also said in that article:

"Treating the banker as owner of the funds deposited for transmission and his obligation as

> contractual, when he has once acquired a credit for transmitting the funds, any right which the banker thus acquires against his correspondent specifically for the purpose of effecting the transfer may be treated as a quasi-trust fund held for the benefit of his customer. In the *Legniti* case the banker failed before he had taken any steps to procure the credit pursuant to his contractual obligation. *Had he actually acquired the credit and specifically appropriated it or a part of it to his undertaking for account of the plaintiff, a very different situation would have arisen and one on which the plaintiff might properly have based a claim that the credit so far as it was an enforceable one was held by the banker in a fiduciary capacity for the plaintiff.* This was the holding in *Farley* v. *Turner*, where the banker had established a credit with his correspondent and instructed his correspondent to pay the third person. Thereafter the bank stopped payment. The credit was cancelled and the proceeds of the credit were received by one of the bankers who was liquidating the business. It was held that the money thus received was a quasi-trust fund, although the English courts hold that the money when deposited with the banker for transmission, does not constitute such a fund, the bank being a general debtor. *In a few cases a similar result has been reached on similar reasoning. And in others involving a similar transaction this result has been properly reached, although the court placed its decision on the ground that the money when deposited constituted a quasi-trust fund.*"

Thomas B. Paton, Esq., General Counsel of the American Bankers Association, and a recognized authority on question of banking law, to whom member banks of that association refer legal problems arising in the course of

their business, has considered the very question presented in this case.

In Vol. 16, No. 2 of the Journal of the American Bankers Association (August, 1923), Mr. Paton replied to the following query:

> "An interesting question has arisen as to the status of funds paid to Foreign Banking Houses in New York for the purpose of securing protection of drafts on Foreign Countries drawn by the smaller banks of the interior. Owing to the failure of a prominent concern in New York there are probably a thousand or more small banks interested in this question, and the legal department of our New York correspondent cannot give us any light upon the subject.
>
> "The question is, perhaps sufficiently indicated above but to make it certain I will make the missing question necessary to make it complete. We sent K. N. & K. a remittance to cover a draft which we had drawn on Switzerland. In the meantime and before the presentation of the draft K. N. & K. failed; are we ordinary creditors, or is the money a trust fund which we can claim prior and in preference to General Creditors?"

Mr. Paton's reply includes a careful consideration of the authorities. His conclusions were stated thus:

> "Where money is remitted, as in this case, to a New York Banking House for the specific purpose of being applied to payment of the remitting bank's draft upon Switzerland and is not so applied because of failure of the New York Banking House before presentation of the draft, such money is not a general deposit, for which the New York bank is a mere debtor but is a trust fund for

> which the remitting bank would have preference in the assets in the hands of the receiver. • • •
>
> The principle of the above authorities and others which might be cited applies to the transaction of remittances to K. N. & K. for the purpose of covering drafts drawn by the remitting banks on drawees in foreign countries. The money not having been placed with K. N. & K. as a general deposit subject to check but for the specific purpose of being applied to the payment of drafts drawn by the remitting banks upon other institutions, such money did not become the property of K. N. & K., so as to make it debtor therefor, although it may have been mingled with the funds of that banking house, but it remained a trust fund which can be recovered by the remitting banks from the receiver."

After Mr. Paton's article appeared, the attorneys for the trustee herein addressed a communication to him, which was published in the November issue of the Journal of the American Bankers Association. In this communication, although it concluded with the usual "without prejudice" clause, *the attorneys for the trustee took no issue with Mr. Paton on the proposition that a trust arose from the payment of moneys to the bankrupts under the Drawing Service.* The burden of their letter was that in the headnote to his opinion (in which it was stated that the remitter "is not an ordinary creditor but the money remitted is a trust fund recoverable in full from the receiver") Mr. Paton had neglected to point out that a necessary prerequisite to recovery was the *tracing* of the funds into the receiver's possession.

The attorney for the trustee said:

"In the second paragraph of the body of your opinion, after stating the facts as to the mingling of trust moneys in a general bank account, you state that the courts have held that 'the money can be recovered by the depositor from the receiver so long as it can be traced into the bank's vaults and a sum equal to it is shown to have continuously remained there from the time the money was received by it until the receiver took possession' (citing cases). You will notice that in your head-note above referred to you have made no mention of the necessity for tracing the funds into the receiver's possessiion, and your readers, who most likely have not the time to read the entire opinion, but simply glance at the head-note, have jumped to the conclusion that the mere remittance of their funds for a special purpose entitled them to the immediate repayment of the amount sent from the receiver. They do not seem to be aware of even the single condition which you have attached to their right to recover, to wit: the determination of the existence of a bank balance on the date of the appointment of the receiver as large as, or in excess of, the remittances made by them. * * *

Going further, however, we find ourselves unable to agree with even the body of your opinion quoted above, and for which you cite cases, for the following reasons:

In a case where one remittance for a special purpose has been mingled with the receiver's general bank account, *the sole problem is correctly stated by you to be whether or not, between the time of the receipt of the funds and the time of the tracing proceeding, the receiver's bank balance has continuously been in excess of the amounts remitted and deposited.* But in the present circumstances, where there are thousands of Knauth,

Nachod & Kuhne's drafts and money orders outstanding, for which remittances had been made prior to the receivership and deposited by Knauth, Nachod & Kuhne in the ordinary course of their business, the problem becomes more complicated. *Were the sole question in each case the comparative size of Knauth, Nachod & Kuhne's bank account with each individual remittance, of course, repayment would have to be made by the receiver in the overwhelming majority of cases.* If that rule were followed out, and the receiver in bankruptcy began to make repayments to remitters in the order of their demand, it might very well be the fact that although the bank balances were in excess of any single remittance, those balances were not as large as the total amount of remittances made for which drafts were still outstanding and unpaid. The problem thus becomes a very complicated one for the reason that not only must the total amount of all *priority and trust claims of every nature* be determined before the possibility of the receiver's repaying remitters can be known, but a very detailed schedule must be drawn showing the bank balances of Knauth, Nachod & Kuhne daily for months, or perhaps years before the receivership, and a counter-schedule the amount of trust and priority claims outstanding on each corresponding day.

* * * If we are correct in this conclusion, before any repayment can be made by the receiver in bankruptcy with safety, an omnibus proceeding would have to be started giving all creditors notice to file claims for priority within a certain time, and barring all persons from filing such claims after the time set. The receiver would then be supplied with a list of all possible priority claims *of this trust nature*, and it could then be determined, with the aid of the alleged bankrupts' books,

whether or not such priority claimants were all to be paid *in full*, or to receive a *pro rata* share of their claims because of the reduction of the bank balances below the total amount of their claims, or perhaps some receive their total claims, because of the fact that the bank balances, since their individual remittances, had remained in excess of their claims, and some receive no part of their claim (in priority form) because of the fact that, since their individual remittances, the bank balances had been depleted."

Here we have the position of the attorneys for the trustee, stated deliberately and, no doubt, after careful consideration, with respect to the opinion of the General Counsel for the American Bankers Association, in which he had concluded that a trust arose. The most striking thing about it is that, except for the usual "without prejudice" clause contained in a postscript to the letter, *there is no claim that the fundamental conclusion of Mr. Paton that a trust arose, was erroneous.* The only point which the attorneys for the trustee felt was not satisfactorily covered in Mr. Paton's opinion, was the question of *tracing.* The letter is pregnant with the admission that if a tracing proceeding established the existence of the fund, there is no doubt about the right to reclaim on a trust theory. It can hardly be claimed that the attorney for the trustee in this careful and deliberate letter would have confined his criticism of Mr. Paton's opinion to the question of tracing, if he felt that in addition thereto Mr. Paton had gone wrong on the *fundamental* question in the case—the trust.

THE CASES CITED BY THE ~~APPELLEE~~ Petitioner ARE NOT IN POINT. THEY ALL DEAL WITH SALES OF CREDIT.

It is of course well established that where a banker sells his credit the consideration received by him is not a trust fund. Where, however, the banker receives money for a particular purpose, the money is a trust fund. Although in the present case the claimant did not purchase the bankrupts' credit, the Petitioner relies entirely on cases of purchase and sale of credit. In none of the cases cited by the Petitioner was money delivered to the bank or banker for a particular purpose.

In the *Beecher* case, which is so strongly relied on by the Trustee (Brief, pages 71-74), the plaintiff, as appears from the opinion (page 52) paid money to the trust company in consideration

> "of an agreement by the defendant trust company that it would procure and provide funds in Roumania to meet *the order which it had sold and delivered to the plaintiff*."

The case involved merely the purchase and sale of credit. The plaintiff had bought from the defendant a remittance order, which is similar to a draft, and the case is an authority only in cases of purchases and sales of credit (see *Equitable* v. *Keene*, 232 N. Y., 290, 295).

The Petitioner relies on the *Beecher* case because in the printed receipt given to the purchaser appeared the words: "It is expressly agreed that Cosmopolitan Trust Company acts as agent only for the sender." It will be observed that these words were not contained in any *contract*. They were contained merely in a "receipt"

which was probably a printed form, broad enough in its terms to cover every transaction which might arise, including those in which an agency might exist. The words quoted could not have been intended to apply to the transaction with the plaintiff, because the transaction was a *sale;* there was no "sender" for whom the Trust Company could act as "agent" and no possibility of an agency in the circumstances of the case. In the present case, on the contrary, the provisions for an agency are expressed in a long and carefully drawn *contract,* which is clear and explicit, which is applicable to transactions of the nature of the one here involved *and was drawn expressly for use in such transactions.* The *contract* here is not in the same category with the *receipt* issued in the *Beecher* case, nor are the facts and circumstances of this case similar to those of the *Beecher* case. In the *Beecher* case the bank sold its credit. It drew its *own* draft payable abroad, and in consideration therefor the plaintiff paid his money. In the case at Bar K. N. & K. did *not* draw their own draft (fols. 419, 474). In conformity with the Drawing Service the draft was drawn by the claimant in its own name, "for its own account as principal and our (K. N. & K.'s) name does not appear" (fols. 419, 474). The holder of the draft acquired no rights against K. N. & K. They had, for a consideration, merely agreed to receive a fund provided by the maker of the draft "to cover" its payment and to accept "*employment*" from the maker (fol. 423) as its "*Agent*" to provide the drawee bank "at once" with the money for the payment thereof. The use of these protective clauses was not accidental or inadvertent. They had a very definite purpose in limiting K. N. & K.'s relation to that of an agent; they were guarding against

any responsibility for defaults by the foreign banks after the fund was delivered to them. They were not unfair or unreasonable in taking this precaution because their profit did not justify their assuming any such obligations. We respectfully submit that this is altogether a different case from the sale of credit involved in the *Beecher* case. As the court said, the undertaking of the bank there "was a contract obligation, based upon the payment of the money, to have funds in Bucharest with the bank, which funds should be sufficient to insure the payment of the order on presentation." There was no such obligation on the K. N. & K. here. It was immaterial whether they would have credit with the B. C. I. at the time the draft would be presented. Their obligation was merely to see that the fund with which to pay the draft was delivered to B. C. I., and this obligation they assumed only upon the prior receipt by them of the equivalent amount, plus their charge for the service. They did not even need to have an account with B. C. I. They could provide the fund "by transfer of credit from our balance, *or otherwise*" which means as the Court pointed out in the *Legniti* case "in any form recognized in financial circles." **THE OUTSTANDING POINT ABOUT THE BEECHER CASE AND THE OTHER CASES CITED BY THE PETITIONER IS THAT IN ALL OF THEM THE BANKER DREW AGAINST ITS OWN CREDIT ABROAD AND MERELY UNDERTOOK THAT IT WOULD HAVE A CREDIT BALANCE IN THE FOREIGN DEPOSITORY AT THE TIME ITS ORDER WAS PRESENTED THERE.** Hence the transaction is described as a purchase and sale of credit. In such cases

> "the seller engages that he has the balance at the point on which the payment is ordered" (*Legniti* v. *Bank*, 230 N. Y., at p. 420).

In the present case there is no such situation. There was no representation by K. N. & K. that they had such a credit balance or that they would have such a credit balance on the date of the presentation of the draft and neither Claimant nor the holder of the draft was concerned with that question. The draft was not drawn by K. N. & K. and no recourse could be had against its balance for the payment thereof.

The *Legniti* case cited by the Petitioner (pages 74-76) was also a sale of credit. In that case the plaintiff purchased a cable transfer. In such cases, as the court pointed out (page 420) there is involved

> "a method of transmitting money by cable *wherein the seller engages that he has the balance at the point on which the payment is ordered* and that on receipt of the cable directing the transfer his correspondent at such point will make payment to the beneficiary described in the cable. All these transactions are matters of purchase and sale and create no trust relationships."

There was in our case no engagement by K. N. & K. that they had "the balance at the point on which the payment is ordered" and there was no requirement that they should have it. In our case they merely undertook, as the claimant's agents, to provide the fund abroad with which to pay the draft drawn by the claimant. The court distinctly recognized the distinction between cases calling for the transmission of money abroad and those in which only a credit is purchased (pp. 420-421) and said that in the former cases

> "the bank or transmitter is the agent of the person paying the money, and until the money is sent holds it as agent or trustee for the owner. Such

were the cases of *Musco* v. *United Surety Company* (132 App. Div. 300), and *People ex rel. Zotti* v. *Flynn* (135 App. Div. 276). In these latter transactions the intention of the payer is that the money he gives to his agent shall be sent abroad. It is the amount which he gives that is to be transmitted. *How it is sent may be immaterial to him. If there be time, currency might be purchased and sent. If not, it may be transmitted in any form recognized in financial circles. It is not at all necessary that the sender or agent have credit in the place to which the money is to be sent.*"

These words apply to our case. A certain amount was to be transmitted. How it was sent was immaterial to us. It could be "transmitted in any form recognized in financial circles" and it made no difference whether K. N. & K. had an account there or not.

**ANOTHER IMPORTANT POINT OF DISTINCTION BETWEEN THE CASE AT BAR AND THE LEGNITI AND BEECHER CASES IS THAT IN THOSE CASES THE AMERICAN BANKER WENT INTO BANKRUPTCY BEFORE THE CREDIT WAS ERECTED ON THE OTHER SIDE AND THE FOREIGN BANK NOTIFIED TO PAY THE THIRD PARTY.** In our case the credit was actually erected by B. C. I., at the request of K. N. & K. and the foreign bank was instructed to pay the third party and created the fund with which to do so, long before the bankruptcy. In these circumstances even if the original transmission of the money to K. N. & K. resulted in a contractual obligation only, the appropriation of the money to the undertaking would create a credit held by the foreign banker in a fiduciary capacity for the claimant. Justice Stone has said (21 Col. Law Review, pages 522, 523):

"Treating the banker as owner of the funds deposited for transmission and his obligation as

contractual, when he has once acquired a credit for transmitting the funds, any right which the banker thus acquires against his correspondent specifically for the purpose of effecting the transfer may be treated as a quasi-trust fund held for the benefit of his customer. In the Legniti case the banker failed before he had taken any steps to procure the credit pursuant to contractual obligation. **HAD HE ACTUALLY ACQUIRED THE CREDIT AND SPECIFICALLY APPROPRIATED IT OR A PART OF IT TO HIS UNDERTAKING FOR ACCOUNT OF THE PLAINTIFF, A VERY DIFFERENT SITUATION WOULD HAVE ARISEN AND ONE ON WHICH THE PLAINTIFF MIGHT PROPERLY HAVE BASED A CLAIM THAT THE CREDIT SO FAR AS IT WAS AN ENFORCEABLE ONE WAS HELD BY THE BANKER IN A FIDUCIARY CAPACITY FOR THE PLAINTIFF.** This was the holding in Farley v. Turner, where the banker had established a credit with his correspondent and instructed his correspondent to pay the third person. Thereafter the bank stopped payment. The credit was cancelled and the proceeds of the credit were received by one of the bankers who was liquidating the business. It was held that the money thus received was a quasi-trust fund, although the English courts hold that the money when deposited with the banker for transmission, does not constitute such a fund, the bank being a general debtor. In a few cases a similar result has been reached on similar reasoning. *And in others involving a similar transaction this result has been properly reached, although the court placed its decision on the ground that the money when deposited constituted a quasi-trust fund.*"

In the present case K. N. & K. actually advised the draft abroad, consented to the debiting of its account

with the amount thereof and to the crediting by B. C. I. of its "Drafts Payable" account—an account which was the record of "a special fund awaiting the presentation of any drafts against that fund" (fol. 348)—*and its instructions were actually carried out.*

The Petitioner concedes (page 77) that

> "There is a factual difference between both the Beecher case and the Legniti case and the case at bar"

but argues that in both classes of cases the "underlying obligation" is the same, the difference being merely that in the Beecher and Legniti cases, the obligation was to the customer, whereas in the present case, the obligation was to the inland bank. The difference is deeper than this. In the Beecher and Legniti cases, the banker drew its own drafts and sold them to the purchaser. Its engagement was merely a promissory undertaking that *its own check or draft* would be honored, when presented, *out of the balance it would then have to its credit with the drawee.* The drafts were a sale of the banker's credit and that was what the purchaser bought and paid for and got. When the banker failed to supply the credit, it broke its contract. In our case we did not buy the banker's credit and were not concerned with it. The banker made no representation that it had, or would have, a credit with the foreign bank, and it was not required to have one in order to perform its obligation. No credit in *its* favor would have benefited the holder of the draft, because it was not the drawer. It was required only to provide abroad a fund which the claimant put into its hands, it being selected because it represented that it had better facilities for providing the fund abroad than were

enjoyed by the inland bank. To accomplish this, it entered into the claimants "*employ*" (folio 423) as its "Agent." Furthermore, there is the distinction which Justice Stone pointed out, that in the present case *the fund was actually created and set up on the books of B. C. I.*, whereas in the Beecher and the Legniti cases, the banker suspended before any credit was created abroad for the benefit of the customer.

On page 85, the Petitioner argues that the Legniti and Beecher cases control the situation here. The reason is claimed to be that in this case, the obligation of K. N. & K. was

> "in its essence, solely to see to it that K. N. & K. themselves had a sufficient credit balance with B. C. I. at the time of the presentation of the draft to the debit of which the draft could be paid in pursuance of the directions contained in K. N. & K.'s advice. It was in the consideration of this executory promise that the American Dollars were paid in advance by the Trinidad Bank."

This misstatement of the terms of the drawing service recurs frequently in the Petitioner's Brief and results in a fundamental misconstruction of the relations of the parties. As we have already pointed out, both in the drawing service (folios 420-422) and in the book of foreign drafts (folio 474) it is provided that upon the receipt of the inland bank's advice of the drawing of the draft, and "adequate funds," K. N. & K. will "*promptly*" and "*at once*" notify the foreign bank and provide it with funds for the payment of the draft advised. There is nothing in the record justifying the Appellee's repeated statement that K. N. & K.'s obligation was merely

> "to see to it that it had a sufficient credit balance with the B. C. I. at the time of the presentation of the draft."

As we have already pointed out, drafts drawn under the Drawing Service were not drawn by or payable by K. N. & K. and the drawers were in no way concerned with what credit stood to the account of K. N. & K. Nor is there any support in the record for the statement that the draft, when presented, would *then* be debited against K. N. & K.'s balance. The fact is that K. N. & K.'s balance was debited with the amounts of drafts advised *immediately upon the receipt of the advice by the foreign bank*, and an account kept by the foreign bank under the title "Drafts Payable" was *immediately* credited. It is, therefore, incorrect to say that the drafts were to be debited to the account of K. N. & K. "at the time of the presentation." These distinctions are important because they help mark the difference between the sale of credit and an agreement to transfer a fund.

The *Samuels* case, which is cited on page 78 of the Petitioner's brief, was also a sale of credit. It was a "Mail transfer on London," payable *at the purchaser's option in the future*. Judge Manton, writing for the Court, pointed out (page 885)

> "These are executory contracts for the sale of Pounds Sterling. * * * It is apparent that it was not the intention, or even within the contemplation of the parties that the Appellant would set aside a specified fund of 75,000 Pounds which it would hold for the benefit of the defendant until some time in October, 1920, at which time the defendant might exercise its option and request the appellant to carry out its obligations under the contract."

Judge MANTON also said

> "Two checks were drawn by the appellant (the seller) on its branch in London payable to the defendant on October 29, 1920, two months after the contract was entered into. This was the only evidence in the record that the appellant did anything in connection with the contract for the purpose of its performance. This did not constitute a setting aside of the funds for the purpose of the contract. The contracts were orders by the claimant on its own branch and did not constitute an appropriation of specific money. One's own undelivered check is not regarded as property and of no force and effect whatsoever."

The case was, as Judge MANTON pointed out, a claim upon

> "The breach of *contracts of sale of* 75,000 Pounds at London by the appellant to the defendant."

It bears no analogy to the present case, either upon the facts or the law applicable to it.

The *Toussig* and *Kuehne* cases, cited by the Petitioner on pages 78-80, involved controversies between banks and their depositors. The relation between the parties was simply debtor and creditor. No delivery of money for a particular purpose was involved in these cases and they are inapplicable on their facts.

The Petitioner is particularly emphatic in his reliance upon the case of *National City Bank* v. *Hotchkiss*, 231 U. S. 50, which he urges

> "Recognized the purposes underlying the Trustee's contentions" (Brief, pages 46-47).

That case is totally unrelated to the case at bar on the facts. It involved the right of the defendant to retain

certain securities which the plaintiff, as trustee in bankruptcy, claimed the defendant took as a preferential security, with knowledge of the bankrupt's financial condition. The question there was, whether the securities taken by the defendant were purchased with moneys advanced by the defendant, within the rule existing between banks and stock brokers that where moneys were advanced by the banks the stock brokers held the securities *actually purchased with those moneys* as security for the repayment of the loan. The court held that the securities which had been delivered to the defendant had *not* been purchased with any of the moneys loaned and, therefore, were not held as security under the agreement, even though the moneys loaned had been added "to the general funds" of the bankrupt firm. The portion of the opinion quoted by the trustee will, when read in the light of these facts and circumstances, be seen to be totally inapplicable to the question now before the court. In cases like the one now at bar, as we have already pointed out, it is well settled that there need be no arrangement for the transmission of the actual currency handed over in order that a trust thereof result (*Matter of Fiscal: Legate* v. *Bank, supra*).

***Conclusion with respect to the cause of action based upon the existence of an agency or trust relationship.***

The parties seem to be agreed upon the distinction between "transmission" cases and "sale of credit" cases, and upon the proposition that in the former there is a trust while in the latter there is none. They are not agreed as to within which of the two classes the present

case falls. Yet even within the realm of the disputed question, they are agreed upon one important point, to wit: That the answer must be found in the provisions of the Drawing Service and the acts of the parties under it.

The Petitioner contends that the burden is on the *Claimant* to show, "without vagueness or uncertainty," that a trust or agency relationship follows from the provisions of the Drawing Service. Even if this be the rule, the Claimant has sustained its burden. It is respectfully submitted, however, that the Petitioner has misconceived the rule to be applied in this case, *because here we have a written agreement which expressly provides for an agency and trust relationship*, and it is the Petitioner who seeks to put upon the transaction a construction *different from the one expressed in the agreements*. In these circumstances, we submit, the burden is on *him*.

The written agreement was drawn with care and deliberation by K. N. & K. Presumably they have put it in the form most favorable to them and it is to be construed against them wherever the construction is open to doubt.

We start off, then, with the proposition that K. N. & K. invited the inland banks to deal with them, upon terms selected by them. They provided that the inland banks should draw drafts in their own names, upon foreign banks to be selected from a list furnished by K. N. & K. They provided that their name was not to appear on the draft. They recognized that this would make it necessary *for the inland bank* to provide a fund, sufficient to meet *its* draft, in the hands of the drawee. They recognized also that small inland banks lack the facilities with which to provide such funds abroad, and they offered, *for* a consideration, and upon the prior receipt of an

"adequate" amount "to cover" the draft, to cause the fund to be provided abroad for them. However, for the small fee involved, K. N. & K. were not assuming any responsibilities for the acts, omissions or derelictions of the foreign banks. They confined their obligation to "providing the drawee banks with sufficient funds to cover" the payment of drafts, and thereupon their responsibility ended. It was only natural that K. N. & K. should so restrict their liability because for the small fee which they got for their services they could not afford to become guarantors of solvency and performance by the foreign bank. The language which K. N. & K. chose clearly and unmistakably carried out their purpose. They provided that the inland banks would "issue their own drafts as PRINCIPALS," "our (K. N. & K.'s) name not appearing thereon;" they then provided that the inland bank should immediately forward to them a sum, computed on a basis fixed by them, which would be sufficient to provide the fund abroad and, in addition, pay them their compensation. They next provided for an "employment" by which

> "we are *employed merely as the agents* of the drawers for the purpose of advising the issue of their drafts and providing the drawee banks with sufficient funds to cover their payment."

and this relationship they emphasized (fol. 475) by repeating that their "sole function" was

> "to advise the drawees of the issue of drafts drawn by our correspondents and to provide for payment, *in which function we act as agents of the drawees.*"

Having described the nature and the purpose of the agency and the terms upon which they agreed to undertake the agency, K. N. & K. provided for the method of performance to wit, that upon receipt of advice from the inland bank of the drawing of a draft, accompanied by

> "adequate funds to cover such drafts at the rates quoted by us for the day on which the drafts are sold"

they would "promptly" and "at once" forward their advice to the drawee bank

> "and provide the drawee with funds sufficient for thepayment of the draft abroad."

We respectfully request the Court to consider what other language K. N. & K. could have employed for the purpose of limiting their obligation to that of a mere *conduit* though which the money, provided by the inland bank for the payment of its draft abroad, would be put into the possession of the foreign bank which was to pay the draft.

It becomes apparent that K. N. & K. was most circumspect in the choice of its language, and in clear, unequivocal and express terms, limited their liability to that of anintermediary, whose sole obligation was, "*as agent" forthe inland bank*, to put in the hands of the foreign bak the equivalent of the fund given to it by the inland ban for that purpose, *—and thereupon to be relieved of al further responsibility.*

The Trustee, by a labored and forced construction, now contends that the bankrupts undertook much greater responsibilities. Indeed, he even urges that if the foreign bankswent bankrupt after K. N. & K. created the

fund in their hands, the obligation would *still* remain upon K. N. & K. to see that the draft was paid and it would, therefore, have to put up the money a second time. Obviously, there was no such obligation. K. N. & K. supplied a list of foreign correspondents. It made no representations or warranties of their financial responsibility and it undertook no obligation in that regard. **THE SUGGESTION OF THE TRUSTEE THAT, FOR THE SMALL COMPENSATION THEY RECEIVED, K. N. & K. WERE GUARANTEEING THE CONTINUED FINANCIAL RESPONSIBILITY OF THE HUNDREDS OF FOREIGN CORRESPONDENTS MENTIONED IN THEIR LIST THROUGHOUT THE PROTRACTED PERIOD WHICH WOULD INTERVENE BETWEEN THE ISSUE OF THE DRAFT AND ITS PRESENTATION, AND THAT THEY WERE ALSO GUARANTEEING DUE PERFORMANCE BY THE FOREIGN BANK OF ITS OBLIGATION TO PAY, IS TOO PATENTLY SPECIOUS TO MERIT SERIOUS CONSIDERATION.** The Trustee's magnanimous offer to permit such a construction is an empty gesture, requiring but little courage, *now that it is K. N. & K., and not the foreign bank, that is in bankruptcy.* Of one thing we may be certain, however, and that is that if K. N. & K. were not in bankruptcy, they would stand for no such proposition. They would be quick—and rightfully so—to refer to the terms of the Drawing Service, to emphasize that they were only "employees" of the inland bank, for whom they acted only as "agents"; that in return for the trifling charge which they made they could not be expected to guaranty the solvency of, and the performance by, the foreign banks, and to claim their immunity from responsibility for the acts or omissions of the foreign banks, once they had put into the foreign bank "a sum sufficient to cover" the payment of the draft.

## POINT III.

**Funds delivered to one in trust may be recovered by reclamation where the Trustee goes into bankruptcy without applying the property to the use for which he received it, providing the same can be traced.**

We take it there can be no serious dispute about the proposition stated above. If authorities were required, a mere reference to the authorities cited under Point II, *supra*, and

> *National Bank* v. *Ins. Co.*, 104 U. S. 54;
> *Surety Co.* v. *Carroll*, 194 Fed. 593, and
> *In Re Schmidt*, 298 Fed. 314,

would more than suffice.

We have already shown that K. N. & K. was a trustee of the claimant's money and did not apply it to the accomplishment of the purpose for which it had been given. There remains only the question: Can the money be traced?

## POINT IV.

**It is conceded that K. N. & K. did in fact create the fund which they agreed, under the terms of the drawing service, to create. The fund abroad was but a transmuted state of the money remitted by Claimant to K. N. & K. It was subject to the same equities. Upon the return of the money to the Receiver, at his request, and with knowledge of the Claimant's equities, the money stood in the place of the original remittance and the Receiver held it upon the same trust as Knauth, Nachod & Kuhne had held the original remittance.**

We are not concerned here with intervening rights of third parties. The present holder of the fund enjoys no equity or immunity except such as K. N. & K. would have enjoyed if they, and not the Trustee, had procured the foreign bank to return the funds to them.

We submit that a mere statement of the facts must lead to the conclusion that if, having received the money under the terms of the Drawing Service, K. N. & K. had carried out its obligation to the extent of providing the fund abroad and had then, without cause, procured that fund to be returned to it, K. N. & K. would have had no shadow of a defense to a claim by this claimant for a return of its money. What better position in this Court of Equity can the Trustee claim?

It may be argued that because the particular dollars which the claimant remitted to the K. N. & K. are not shown to be the very dollars which the foreign bank

returned to the receiver, the claimant cannot trace into the fund returned. Any such contention would be contrary to reason, as well as to judicial precedent.

The claimant remitted money for a particular purpose and K. N. & K. accepted it for that purpose. Whether K. N. & K. used the very money so received to comply with that purpose or whether they put that money in a bank and took other money from the same or another bank to comply with the purpose is immaterial. *They did, in fact, proceed to carry out the purpose by actually creating the fund abroad.* That fund, when created, took the place of the money which the claimant had remitted to the bankrupts, and, as between the claimant and the bankrupts, that fund remained the medium for the carrying out of the purpose. K. N. & K., we must assume—because the Trustee stands only in the shoes of the bankrupts—thereafter proceeded to transfer the fund to themselves here. We submit that it would be contrary to equity and good conscience to say that this money, so procured and still in the hands of the bankrupts, is free from any equities which existed against the money theretofore. It would also be contrary to the authorities, because the cases make it clear that funds substituted for trust funds themselves become trust funds; that in dealing with *money*, the right to follow does not depend upon the identification of the particular dollars placed in trust, but that where the trust moneys have been transmuted into something else, and can be traced into it, the trust will attach to the resulting fund.

*Perry on Trusts*, 6th Ed., Sec. 828;
*May* v. *LeClaire*, 11 Wall. 217;
*Hutchinson* v. *LeRoy*, 113 Fed. 202;

*American Sugar Refining Co.* v. *Fancher*, 145 N. Y. 552;
*Welch* v. *Polley*, 177 N. Y. 117;
*Gorman* v. *Littlefield*, 229 U. S. 19;
*Duel* v. *Hollins*, 241 U. S. 523.

*Perry on Trusts*, 6th Ed., Sec. 828.

> "Trust property *or property substituted for it* may be recovered from the trustee and all persons having notice of the trust. So long as the fund can be distinctly traced the chancellor will follow it and fasten the purpose of the trust upon it, unless the rights of innocent third parties have intervened."

In *May* v. *La Claire*, 11 Wall. 217, the Court said:

> "At law, in many cases if property be tortiously taken or converted, the tort feasor may be sued in trespass or trover, or the injured party may waive the tort and sue in *assumpsit*. In the latter case the same results follow as if there had been an implied contract. * * * In the same class of cases, where the converted property has assumed altered forms by successive investments, the owner may follow it as far as he can trace it and sue at law for the substituted property, or he may hold the wrongdoer liable for appropriate damages. There are kindred principles in equity jurisprudence, whence, indeed, these rules of the common law seem to have been derived."

In *Hutchinson* v. *LeRoy*, 113 Fed. 202, the Circuit Court of Appeals said (p. 206):

> "As, according to equitable principles, these equities attached to the fund, it followed it, of course, wherever it could be found, until it should reach the hands of an innocent purchaser for value. The proposition of the trustee in bank-

ruptcy that it cannot be determined out of what portion of the proceeds the loan of the Beacon Trust Company was paid, and that therefore it cannot be said that LeRoy had any lien on the specific surplus remaining after payment of the loan, is one nowhere recognized.

"The efficiency of the rules of the chancery courts, by virtue of which LeRoy seeks to impress the surplus in the hands of the Beacon Trust Company with equities in his behalf, is peculiarly illustrated by an extensive class of authorities, of which the opinion of Mr. Chief Justice Gray in *Bank* v. *Barry*, 125 Mass. 20, is a noteworthy one. There the money in question was taken by a clerk of the bank, yet not in his capacity as clerk. It was stolen. A part of it was delivered by him to one Barry, who was a stranger to the bank, and who with it purchased land, taking the title in the name of his mother; and Mr. Chief Justice Gray, delivering the opinion in behalf of the court, said that equity would charge the land with a trust in favor of the bank for the money received by Barry, it appearing that he knew that it was stolen. Thus, although the money was stolen in the form of currency or coin, and although it had gone through two hands, equity so ear-marked it as to follow it into the real estate in question."

Chief Judge Andrews, writing for the Court of Appeals, *American Sugar Refining Co.* v. *Fancher*, 145 N. Y. 552, said page 556:

"The jurisdiction of a court of equity to follow the proceeds of property taken from the true owner by felony, or misapplied by an agent or trustee, and converted into property of another description, and to permit the true owner to take the property in its altered state as his own, or to

hold it as security for the value of the property wrongfully taken or misapplied, or, in case the original property or its proceeds have been mingled with that of the wrongdoers in the purchase of other property, to have a charge declared in favor of the person injured to the extent necessary for his indemnity, so long as the rights of *bona fide* purchasers do not intervene, has been frequently exerted and is a jurisdiction founded upon the plainest principles of reason and justice. * * * The cases upon this head are very numerous, where there has been a misapplication of trust funds by trustees, or persons standing in a fiduciary relation, and the money or property misapplied has been laid out in land or converted into other species of property. The court in such cases lays hold of the substituted property and follows the original fund, through all the changes it has undergone, until the power of identification is lost or the rights of *bona fide* purchasers stop the pursuit, and holds it in its grasp to indemnify the innocent victim of the fraud. And even in case of money, which is said to have no earmark, its identity will not be deemed lost though it is mingled with other money of the wrongdoer, if it can be shown that it forms a part of the general mass. (*Pennell* v. *Deffell*, 4 DeG. M. & G. 372; *In re Hallett*, 13 Ch. Div. 696; *Holmes* v. *Gilman*, 138 N. Y. 369). * * *

* * * It is claimed that the general creditors of the firm will be prejudiced if the plaintiff is allowed to prevail, and that he will thereby acquire a preference over the other creditors of the insolvent firm. But general creditors have no equity or right to have appropriated to the payment of their debts the property of the plaintiff, or property to which it is equitably entitled as between it and Burkhalter & Co. They, so far as

appears, advanced nothing and gave no credit on the faith of the firm's possession of the sugars, assuming that that element would have had any bearing on the case. If the sugars had existed in specie in the hands of the assignee it cannot be doubted that the plaintiff on rescinding the sale would have been entitled to retake them, and the general creditors are in no worse position, if the plaintiff is awarded the proceeds, than they would have been if the sugars had remained unsold. • • •

When these legal remedies are available and adequate, clearly there is no ground for going to a court of equity. The legal remedies in such case are and ought to be held exclusive. But in a case like the present, where there is no adequate legal remedy, either on the contract of sale or for the recovery of the property in specie, or by an action of tort, is the power of a court of equity so fettered that where it is shown that the property has been converted by the vendee and the proceeds, in the form of notes or credits, are identified beyond question in his hands, or in possession of his voluntary assignee, it cannot impound such proceeds for the benefit of the defrauded vendor? The only reason urged in denial of this power, which to our minds has any force, is based on the assumption that it would be contrary to public policy to admit such an equitable principle into commercial transactions. But with the two limitations adverted to, and which ought strictly to be observed, (1) that it must appear that the plaintiff has no adequate remedy at law, either in consequence of insolvency, the dispersion of the property or other cause, and (2) that nothing will be adjudged as proceeds except what can be specifically identified as such, business interests will have adequate protection."

Judge Edward T. Bartlett, writing for the Court of Appeals in *Welsh* v. *Polley*, 177 N. Y. 117, said, page 122:

> "In view of the facts disclosed by this record, it was proper for the plaintiff to institute a suit in equity, bringing in her defaulting trustee, the bankrupt, and his trustee in bankruptcy as parties defendant. In that suit the plaintiff was entitled to prove, if she could, that a certain portion of the trust fund held by Polley went into the purchase price of the real estate transferred to Cavanagh, and assuming, as we must, that the sum received by the trustee in bankruptcy, in compromise of the judgment recovered by him, declaring the conveyance of the bankrupt to Cavanagh fraudulent, stood in the place of the property, which might have been reconveyed to the trustee in bankruptcy, she would be entitled to have restored to the trust such portion of that fund as she was able to successfully follow into the purchase money paid by the bankrupt, or into the funds in the hands of the trustee in bankruptcy.
>
> • • • • • • •
>
> "The plaintiff must be permitted to follow, if she can, her trust moneys into the hands of the trustee in bankruptcy, he having no greater right against her than the bankrupt, her trustee, possessed had he remained solvent.
>
> The other creditors of the bankrupt have no claim upon any of the funds derived from plaintiff's trust which can be fully identified.
>
> To the extent that plaintiff is able to follow trust funds into the purchase price of the real estate, or into the bankrupt's estate generally, she points out moneys that are no part of the estate held by the bankrupt's trustee for general distribution among the creditors, and is entitled to have them restored to the trust for her benefit which is to continue during her life."

The authorities to which we have referred establish the right of the claimant to reclaim against the funds returned to the receiver by Banca Commerciale Italiana. They show:

(1) That K. N. & K. received the claimant's money in trust to use it for a particular purpose.

(2) The fund for the creation of which Claimant delivered its money to K. N. & K. was created by K. N. & K., but, before it was used for the purpose intended, the fund was taken back by K. N. & K.'s Receiver and by him turned over to the Trustee, in whose possession it remains.

(3) The money returned by the bank abroad stands in the place of the money paid by the Claimant to the Bankrupts; it is "property substituted for" the trust property and as such may be followed and recovered.

## POINT V.

**The claimant agrees with the Petitioner that the rights of the parties became fixed upon the filing of the petition in bankruptcy and that the subsequent acts of the Receiver cannot change those rights.**

The Petitioner points out (brief, pp. 87 *et seq.*) that the rights of the parties become fixed upon the filing of the petition in bankruptcy and that the subsequent correspondence between the receiver and B. C. I. cannot change those rights.

The burden of the trustee's fourth point, in which this subject is discussed, is that the correspondence shows that the parties recognized that K. N. & K. was a creditor of B. C. I. even with respect to amounts charged in the "Drafts Payable" account. The correspondence permits of no such construction. We have already discussed the communications which passed between the receiver and B. C. I. and we shall not extend the pages of this brief by referring to them again, further than to repeat that B. C. I. promptly notified the Receiver that moneys in the Drafts Payable account were *not* the property of K. N. & K. (Claimant's Ex. 11), and that it was only after the receiver wrongfully notified B. C. I. to "*cancel all drafts charged but not paid before receivership*" that the money which had been set aside by B. C. I. in the "Drafts Payable" account to meet these drafts was "re-credited" to K. N. & K. and returned to him with a communication which definitely ear-marked the returned money and the particular drafts for the payment of which it had been held by B. C. I. B. C. I. certainly had a right to assume, from the communications received from the receiver, that the necessary condition precedent to cancellation of drafts, as testified to by the trustee's witness (fol. 351), "that the drawer bank wants to cancel," existed. But, whether B. C. I. had the right so to assume or not, it is sufficient for the determination of this case that K. N. & K., and its receiver, had *no right* to cancel drafts advised unless "the drawer bank wants to cancel," and that the drawer bank in this case did *not* "want to cancel." The receiver was not within his rights in cancelling the draft and having, in violation of right, procured possession of the fund which had been set apart by B. C. I. to pay the draft, he holds the money so received as the property of the holder of the drafts.

Section 70 of the Bankruptcy Law, dealing with the classes of property which pass to a trustee, to which the

Petitioner refers on pages 87 and 88 of his brief, has nothing to do with the case. The *bankrupts* had no right to cancel the claimant's draft and, consequently, the *trustee* acquired no such right.

Nor is there any attempt here to disturb the equality which must exist between all creditors of the same class (Petitioner's Brief, pp. 89, 90). All Claimant asks is that money which belongs to it, *and which is not part of the Bankrupt estate*, should not be diverted from it for the benefit of others, who are not entitled to it.

## POINT VI.

**K. N. & K. received the Claimant's money as the Claimant's agent, upon a trust to apply it to a particular purpose. The trust not having been executed and the money now being in the Trustee's hands, the Claimant is entitled to its return.**

**Irrespective of whether the money was originally received by K. N. & K. as a trust fund, the Claimant is entitled to recover because the Trustee has received, with knowledge of the Claimant's rights, a fund which was equitably assigned by K. N. & K. for the payment of the draft involved in this proceeding.**

**The decree of the Circuit Court of Appeals should be affirmed.**

Respectfully submitted,

William DeForest Manice,
Attorney for Petitioner-Appellant.

William DeForest Manice,
Allen R. Memhard,
George Thorn,
Of Counsel.

No. 130

FILED
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# Supreme Court of the United States

THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy of Knauth, Nachod & Kuhne,
*Petitioner,*

*against*

THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO,
*Respondent.*

## PETITION OF RESPONDENT FOR RE-HEARING

WM. DE FOREST MANICE,
*Counsel for Petitioner.*

# SUPREME COURT OF THE UNITED STATES.

No. 130.—October Term, 1927.

The Equitable Trust Company of New York, Trustee in Bankruptcy of Knauth, Nachod & Kuhne, Petitioner,

vs.

The First National Bank of Trinidad, Colorado.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[January 3, 1928.]

Mr. Justice Holmes delivered the opinion of the Court.

Knauth, Nachod and Kuhne being in bankruptcy, the respondent, The First National Bank of Trinidad, Colorado, claimed priority in respect of certain funds collected by the trustee in bankruptcy, the petitioner, from the Banca Commerciale Italiana; the ground of the claim being that these funds were charged with a trust in the hands of the Italian bank. The respondent prevailed in the Circuit Court of Appeals. 13 F. (2d) 732. A writ of certiorari was granted by this Court. 273 U. S. 684.

The facts are as follows. The bankrupts had credit with many foreign banks and to enable small banks in this country to issue drafts upon such banks in their own name offered these terms: "Upon receipt of advice of draft, accompanied by adequate funds payable at par in New York, we shall promptly forward our advice of the same and provide the drawee with funds sufficient for the payment of the draft abroad, by a transfer of credit from our balance, or otherwise, provided the draft is drawn on a bank named in our latest list of correspondents." It was added that the drawing banks act as principals and draw in their own name, the bankrupts being employed merely "as agents of the drawers for the purpose of advising the issue of their drafts and providing the drawee banks with sufficient funds to cover their payment."

The bankrupts sent out lists of their foreign correspondents and also daily rate cards fixing the rate for the various foreign currencies, including their own compensation, good only for the day of the date. In accordance with this plan the Trinidad bank drew a draft on a branch of the Banca Commerciale Italiana for 24360 lire, sent notice to the bankrupts that they had sold it "and shall thank you to protect same upon presentation," and remitted therewith a check for $1,191.20, which the bankrupts received on May 22, 1923, and deposited to their general account. On the same day the bankrupts sent to the Italian bank and to its branch a list and description of the drafts issued by inland banks and by the bankrupts and requested it to "honor the above listed drafts charging same to our account." The list was received on or before June 4, 1923; the account of the bankrupts was debited with the total amount and to that extent ceased to draw interest, the bank getting its compensation in this way. At the same time an account termed "Drafts Payable" was credited with the same amount, this account being credited in the same way with drafts from other dealers with the bank and the bankrupts themselves. In accordance with the practice in international banking, the bankrupts when they saw fit to do so cancelled their advices and were recredited in their general account; and although in fact they did not cancel the advice of inland drafts except when requested by the inland banks, the Italian bank did not know or inquire into reasons and so far as appears the Trinidad bank or at all events the holder of the draft knew nothing of the mode of bookkeeping described.

The draft was presented after the petition in bankruptcy had been filed and was dishonored; the petitioner as drawer had to take it up and now claims on the two grounds that the sum paid by it was paid upon trust to be applied to the draft, and that as holder of the draft it is, by subrogation, an equitable assignee of the bankrupts' deposit with the drawee. The first of these need not detain us. *Beecher* v. *Cosmopolitan Trust Co.*, 239 Mass. 48. *Legnis* v. *The Mechanics & Metals National Bank*, 230 N. Y. 415. The identity of the fund was not maintained and no one expected it to be. *See National City Bank* v. *Hotchkiss*, 231 U. S. 50, 56, 57. The bankrupts undertook to 'forward' advice but only to 'provide' the drawee with funds. The second contention was that which prevailed below. Of course there is room for difference

if the parties did not express very clearly what they wanted or meant but we are led to a different conclusion whether the reliance be upon the rights of the holder or upon the original contract between the respondent and the bankrupts. In the first place the ignorance of the whole affair on the part of the holder and the general understanding that the party dealing immediately with the bank having the 'Bills Payable' account is master of it, as between himself and the bank, are quite inconsistent with the notion that an entry on that account is the appropriation of a fund to the holder's use. The respondent tries to give a different turn to the evidence but the master's finding and our own conclusion from the testimony leave no doubt in our minds. It is true that after such an entry the interest allowed to the depositor stops but that is only a convenient way of giving compensation to the bank. It is not uncommon in commercial transactions to see some of the elements of an earlier or a half imitated transaction appear, although the essentials of the transaction are not there. Whether a fund was appropriated or not depended wholly on the dealings between the bankrupts and the Italian bank; and both of them dealt with the account as subject to the bankrupt's control. The cessation of interest was for the benefit of the bank because the account was only with its general funds, and did not have any assets especially set aside and appropriated to it—in short was a bookkeeping device for the convenience of the bank.

Again, the terms offered by the bankrupts to their correspondents seem to us to promise the appropriation of a specified fund to the draft as little as they promise to apply the money received by them to that end. They are to provide the drawee banks with sufficient funds for the payment of the drafts by transfer of credit from our balance 'or otherwise'. They are to provide, that is, as convenient to themselves, for payment by the drawee banks, not to give them an earmarked corpus to be handed over. They are requested by their correspondents to protect the drafts, which again means merely to see that they are paid. *Wabash, St. Louis & Pacific Ry. Co.* v *Ham*, 114 U. S. 587, 596. People dealing with large banks do not ordinarily seek the ambiguous security of an identified fund, they are satisfied if the bank gives them credit. We see no indications that the Trinidad bank was not perfectly

content to know that it would have credit with the Banca Commerciale, and that in the usual course of things its drafts would be paid. Evidently with this conception of their duties the bankrupts asked the Italian bank "to protect to the debit of our account the drafts" in question and others, and the branch bank to "honor the above listed drafts." That such a letter of advice is not an assignment is clearly explained in *Eastman Kodak Co.* v. *National Park Bank*, 231 Fed. Rep. 320, 323; (affirmed, 247 Fed. Rep. 1002.)

We have called the instrument under which the respondent claims as assignee, a draft. But on its face it is called 'check'. The form was a general form furnished by the bankrupts and the purpose is said to have been that in continental Europe or some parts of it checks are not subject to the same stamp tax as drafts. It is said in a reputable work that the fact that the instrument purports to be drawn upon a deposit is what constitutes it a check. Daniels, Negotiable Instruments, 6th ed., § 1569. The existence of this opinion sufficiently explains the words of the document before us 'Pay from balance against this check'. They no more purport to assign a fraction of a fund than does an ordinary check. They would not naturally take that shape as the respondent, the drawer of the check, had no fund in the hands of the drawee.

The decision of this case depends more upon the general import of the transaction and upon what the parties were likely to want than upon the phrases that can be picked out from the several steps. We repeat that in our opinion what the parties meant to establish and what the respondent got was the assurance of a credit abroad to the extent of its check as in the case of a letter of credit, not an attenuated property right in an account to which no special funds were attached and the particulars of which neither the respondent nor the purchaser of the check could know.

*Order reversed.*

A true copy.

Test:

*Clerk, Supreme Court, U. S.*

# SUPREME COURT OF THE UNITED STATES.

No. 130.—October Term, 1927.

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|---|---|
| The Equitable Trust Company of New York, as Trustee in Bankruptcy of Knauth, Nachod & Kuhne, Petitioner, *vs.* The First National Bank of Trinidad, Colorado. | On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit. |

[January 3, 1928.]

Mr. Justice Stone, dissenting.

The agreement of the bankrupts, on the faith of which petitioner sold its draft, did more than stipulate that the draft should be paid on presentation. It provided specifically the method of payment; that the bankrupts should "promptly", on notice of the draft, "provide the drawee with funds sufficient for the payment of the draft abroad, by a transfer of credit or otherwise." It plainly contemplated the course of business, actually followed, in which a credit, to be established with the drawee, was to be set apart and specifically appropriated to the payment of the draft. The draft was by its terms made payable from "balance against this Check".

We need not discuss what the petitioner's rights would have been if no such credit had been established, for here the bankrupts had performed their contract fully and to the letter. They set apart the stipulated credit. Withdrawal of it by them would have been a violation of their contract with petitioner, for the contract contained no intimation of a right to revoke it, and if the receiver had not done what they had no right to do the draft would have been paid. Nor does it appear to me that the real question is whether the Italian bank was charged with a trust with respect to funds lodged with it by the bankrupts. It may be assumed that it was not a trustee, but only a debtor to the bankrupts for the funds thus received, with power to discharge the debt *pro tanto* by payment of the draft when presented.

Stated with precision the question seems rather to be whether, since the bankrupts had performed their agreement by specifically designating and setting apart enough of their credit with the Italian bank to meet the draft, the credit thus set apart is to be treated in equity as security for the payment of the draft. If subject to that equitable obligation, neither the bankrupts nor the receiver could convert the credit, so set apart, into cash and turn the proceeds over to general creditors freed of that obligation.

Since *Holroyd* v. *Marshall*, 10 H. L. Cas. 191, it has been generally accepted doctrine, the recording acts permitting, that an agreement to hold property which the promisor may afterward acquire as security for the payment of a debt, operates in equity once the property is acquired, to give the stipulated security to the promisee in preference to general creditors. Such is the rule in this Court. *Sexton* v. *Kessler*, 225 U. S. 90. I had supposed it to be equally well settled that the agreement need not mention the word "security" to accomplish that result, if its plain purpose is to provide for the satisfaction of a debt or obligation out of identifiable property. Compare *Walker* v. *Brown*, 165 U. S. 654; *Ingersoll* v. *Coram*, 211 U. S. 335; *Hurley* v. *Atchison, Topeka & Santa Fe Ry.*, 213 U. S. 126; *Ketchum* v. *St. Louis*, 101 U. S. 306; *Parlin & Orendorff Implement Co.* v. *Moulden*, 228 Fed. 111; *Curtis* v. *Walpole Tire & Rubber Co.*, 218 Fed. 145. There has been no dissent from the view that an agreement to apply a designated credit or account to the payment of a check or draft drawn upon it creates security in the credit enforcible in equity as against general creditors. *Fourth Street Bank* v. *Yardley*, 165 U. S. 634; *Farley* v. *Turner*, 35 L. J. Ch. 710; *Coates* v. *First National Bank*, 91 N. Y. 20; *Muller* v. *Kling*, 209 N. Y. 239; *In re Hollins*, 215 Fed. 41. Equity, in making such agreements effective, does no more than it habitually does in compelling the performance of an agreement to give a mortgage to secure advances made on the faith of the agreement.

Both parties to this transaction knew that American drafts drawn on European banks would be worthless unless definite arrangement for their payment by the drawee was made in advance of their presentation, and that where, as here, a particular credit was set apart for that purpose the utility of such drafts would

be seriously impaired if the credit, once established, could be cancelled at will. No intelligent banker would sell such drafts if the establishment of such a credit were not contemplated. A bank here, drawing and selling such drafts against a credit to be established abroad by others, pledges its own credit to the payee and is secured against loss and the dishonor of its drafts only in so far as it may insure the creation of the appropriate credit and retain the benefit of it once it is created. The stipulation that the bankrupts should promptly set apart a credit for that purpose upon receipt of advice of the draft and advise the drawee of it was a material inducement to petitioner to pledge its own credit by the sale of its draft. Once performed it is valuable security to both payee and drawer, if it is permitted to have the legal sanctions which ordinarily attach to agreements of this character.

The evidence in this case appears to me, as it did to the court below, to fall far short of establishing a practice or custom, or any rule of Italian law, permitting the depositor, while the drafts are outstanding, to cancel or control for his own purposes the credit set apart for their payment. Our own rule is that a bank of deposit may not, with impunity, ignore the known equitable rights of others to the credit established by its depositor, *National Bank* v. *Insurance Co.*, 104 U. S. 54, and it would seem that that rule should be applied here in determining the rights of the parties in the absence of proof of any other. But in any case, such control, if retained by the bankrupts as between themselves and the Italian bank, could not be rightfully exercised in violation of their contract with petitioner.

The case would therefore seem to be a proper one for the application of the rule announced by this Court in *Fourth Street Bank* v. *Yardley, supra*, that a court of equity will lend its aid to carry into effect an agreement that an obligation shall be satisfied out of a specified credit. Applied here that rule would make effective the intention of the parties and give stability to a large and important class of banking transactions. The judgment should be affirmed.

Mr. Justice McReynolds joins in this dissent.

# Supreme Court of the United States

| | |
|---|---|
| THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy of Knauth, Nachod & Kuhne,<br>*Petitioner,*<br>*against*<br>THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO,<br>*Respondent.* | PETITION OF RESPONDENT FOR RE-HEARING. |

*To the Honorable, the Justices of the Supreme Court of the United States:*

THE FIRST NATIONAL BANK OF TRINIDAD, COLORADO, respectfully petitions this Court for a rehearing herein and alleges:

1. Knauth, Nachod & Kuhne (hereinafter referred to as "K. N. & K."), commercial bankers in the City of New York, entered into a contract, known as the "Drawing Service", with respondent, a bank in Colorado. The contract was drawn by K. N. & K. It covers about twenty pages of the record and is particularly specific in its provisions governing the relations of the parties to one another. It provides that respondent should draw drafts on foreign banks *in its own name;* that respondent should then forward to K. N. & K. a sum, as fixed by K. N. & K., to produce the necessary amount of foreign currency to cover the draft and, in addition, to compensate K. N. & K. for its services in the matter, and that upon receipt thereof K. N. & K. would "promptly" and

"at once" advise the foreign bank of the draft which respondent had drawn and provide it with funds to pay the same. K. N. & K.'s statement of their relation to the transaction is stated in the contract as follows (fol. 423):

> "Under this arrangement our correspondents in this country act as Principals, and issue drafts in their own name, our name not appearing thereon. *In other words, we are employed merely as the agents of the drawers for the purpose of advising the issue of their drafts and providing the drawee banks with sufficient funds to cover their payment.*"

2. These are the provisions of the contract, the language of which was selected by K. N. & K.

Under this contract the respondent drew its draft on Banca Commerciale Italiana (hereinafter referred to as "B. C. I.") and thereupon forwarded to K. N. & K. an advice of the drawing of the draft, accompanied by adequate funds, all as provided in the terms of the Drawing Service. This draft was taken from a book of drafts supplied by K. N. & K. and distributed by them as part of the Drawing Service, on the cover of which book K. N. & K. reiterated (fols. 474-475):

> "Under this arrangement our correspondents draw drafts for their own account, as Principals, and our name does not appear, our sole function being to advise the drawees of the issue of drafts drawn by our correspondents and to provide for payment, *in which function we act as agents of the drawers.*"

3. "Promptly" upon K. N. & K.'s receipt from respondent of its advice of the drawing of its draft, accom-

panied by adequate funds to cover, K. N. & K. advised B. C. I. thereof, giving the amount and other identifying particulars thereof, and directed B. C. I. to charge the same to their account and honor the same, knowing that, under the universal custom, B. C. I. upon receipt of these instructions, would charge their account with the amount of the draft and credit that amount to its own Drafts Payable account, which was an account maintained by B. C. I. representing funds set aside to await the presentation of the drafts therein described. Thereupon, K. N. & K. ceased drawing interest on the amount so taken out of their account and no longer treated that amount as any part of their assets. K. N. & K. thereupon regarded their performance as complete, as appears from the fact that they were not concerned to know whether the draft was ever presented or not, *i. e.*:

> "Payment of drafts abroad is not usually reported to us; and we can only ascertain whether or not drafts have been presented for payment by making special inquiry of the drawee bank" (fol. 433).

4. The money transferred to B. C. I.'s Drafts Payable account remained there until the receiver in bankruptcy of K. N. & K., before the draft was presented, sent word to B. C. I. to cancel the draft drawn by respondent and thus procured B. C. I. to recredit to the account of the bankrupts, and remit to him, the moneys which up to that time had been set aside in the Drafts Payable account to meet respondent's draft.

5. Respondent, as drawer of the draft, was subsequently required to refund the amount thereof to its customer and the draft was thereupon assigned to it.

6. The Receiver has been succeeded by the Trustee in Bankruptcy, which holds the funds remitted by B. C. I. to the Receiver.

7. Respondent claimed priority in the fund so returned to the Receiver on two grounds—first, that the money had been received originally by K. N. & K., as agent for petitioner, with which to provide a fund abroad for the payment of its draft and the Receiver had wrongfully prevented the application of the fund to that purpose and procured it to be remitted to him; second, that the money remitted to the Receiver had been equitably assigned by K. N. & K. for the payment of the draft and was, accordingly, not an asset of the bankrupts.

8. The respondent prevailed in the Circuit Court of Appeals (13 F. 2nd 732); a writ of certiorari was granted by this Court (273 U. S. 684) and the order of the Circuit Court of Appeals was subsequently reversed, Mr. Justice Holmes delivering the opinion of the Court, Mr. Justice Stone and Mr. Justice McReynolds dissenting, and Mr. Justice Sutherland taking no part therein.

9. From what the majority of the members of this Court believed was

> "the general import of the transaction and what the parties were likely to want",

it has been held that the money was not paid on a trust to be applied to the draft and that

> "what the parties meant to establish and what the respondent got was the assurance of a credit abroad to the extent of its check".

The last paragraph of the prevailing opinion reads:

> "The decision of this case depends more upon the general import of the transaction and upon

what the parties were likely to want than upon the phrases that can be picked out from the several steps. We repeat that in our opinion what the parties meant to establish and what the respondent got was the assurance of a credit abroad to the extent of its check as in the case of a letter of credit, not an attenuated property right in an account to which no special funds were attached and the particulars of which neither the respondent nor the purchaser of the check could know."

10. The grounds upon which petitioner asks for a rehearing are:

## I.

**The majority of the court were influenced in arriving at the conclusion that there had not been an equitable assignment by the belief that K. N. & K. retained the right to cancel drafts previously advised and thereby procure a re-credit to their own account of the amount previously transferred from their account to the "Drafts Payable" account of B. C. I. This conception of K. N. & K.'s relation to the moneys in the Drafts Payable account is erroneous; K. N. & K. had no such right, except in a limited class of cases, of which the present case is not one.**

In the prevailing opinion it is stated:

"In accordance with the practice in international banking, the bankrupts when they saw fit to do so cancelled their advices and were recredited in their general account; and although in fact they did not cancel the advice of inland drafts except when requested by the inland banks, the Ital-

> ian Bank did not know or inquire into reasons, and so far as appears the Trinidad bank or at all events the holder of the draft knew nothing of the mode of bookkeeping described."

Elsewhere it is said:

> "In the first place the ignorance of the whole affair on the part of the holder and the general understanding that the party dealing immediately with the Bank having the 'Bills Payable' account is master of it, as between himself and the bank, are quite inconsistent with the notion that an entry on that account is the appropriation of a fund to the holder's use."

And later in the opinion:

> "Whether a fund was appropriated or not depended wholly on the dealings between the bankrupts and the Italian Bank; and both of them dealt with the account as subject to the bankrupts' control."

In short, the majority of the Court interpreted the testimony to be that K. N. & K. could cancel a draft already advised "when they saw fit to do so"; that it was "the general understanding" that K. N. & K. remained "master" of moneys transferred from their General Account to the Drafts Payable Account of B. C. I. and that this money remained "subject to the bankrupts' control." This view of K. N. & K.'s rights, coupled with the assumption that neither the respondent nor the original payee could know that B. C. I. would transfer the money to its Drafts Payable Account, appears from the opinion to have been a potent, if not the controlling, consideration which influenced the Court to the conclusion that

there had not been an equitable assignment. With great respect, we submit that the record shows (A) that K. N. & K. did not have the right, "when they saw fit to do so," to cancel drafts which had been advised and that the money in the Drafts Payable Account was not "subject to the bankrupts' control" and (B) that the assumption that respondent and the original payee did not, and could not, know that the fund would be set up in the Drafts Payable Account is erroneous.

## A.

**THE TRUSTEE'S EXPERT—AND HIS TESTIMONY IS THE ONLY TESTIMONY ON THE SUBJECT IN THE RECORD—TESTIFIED THAT UNDER THE GENERAL CUSTOM IN BANKING TRANSACTIONS, K. N. & K.'s RIGHT TO CANCEL AN ADVICE WAS LIMITED TO CASES IN WHICH THE DRAWER OF THE DRAFT REQUESTED K. N. & K. TO HAVE THE DRAFT CANCELLED.**

He testified (fols. 350-352) explicitly that where an inland bank drew a draft, the New York bank could send notice of cancellation in cases where

> **"THE DRAWER BANK WANTS TO CANCEL A DRAFT THAT HAS ALREADY BEEN DRAWN AND ADVISED" (FOLS. 351, 352).**

There is no other testimony on this subject in the record and it is admitted that K. N. & K. never attempted to cancel a draft in any other circumstances (fols. 282-284, 379). The Trustee sought to avoid the effect of this testimony by referring to the statement of Dawson at folio 368 that the question put to him had not included any reference to "a third party" (fol. 368). The question, however, was not framed in terms of "*parties.*" It was framed in terms of *the relation of the actors to*

*the draft*, and the answer applies to *all* transactions, it being immaterial whether there be three, or only two, parties to the transaction. The question was whether there was a general custom with respect to the cancellation of advices and the answer was that K. N. & K. was authorized to send notice of cancellation to B. C. I. in cases where

> "*the drawer bank* wants to cancel a draft that has already been drawn and advised."

The point of the answer was that the *drawer* was the one who had to direct cancellation; that until the *drawer* gave such a direction to K. N. & K., they had no right to send B. C. I. a notice of cancellation. This would, indeed, follow necessarily from the relations of the parties. Respondent being the drawer, K. N. & K. would have no right to cancel the draft, except upon Respondent's direction.

It is admitted that the drawer in this case did not request a cancellation; consequently the notification was wrongful and the Receiver had no right to the return of the money.

The prevailing opinion states:

> "The Italian Bank did not know or inquire into reasons"

for the cancellation; this seems to have impressed the Court with the belief that B. C. I. recognized that the money remained "subject to the bankrupts' control."

*With great respect we submit that this view overlooks the fact that the general custom was known to the for-*

*eign bank*. It knew that K. N. & K. had no right to cancel a draft unless the drawer bank has requested K. N. & K. to do so. It did not need to "inquire into reasons." The custom fixed the only *legitimate* reason and there was no occasion for the foreign bank to doubt that the Receiver, who it knew was an officer of the Court (fol. 525), would not direct the cancellation of a draft if that reason did not exist.

**IN VIEW OF THE CUSTOM—IN THE LIGHT OF WHICH ALL PARTIES MUST BE DEEMED TO HAVE ACTED—THE RECEIVER'S NOTIFICATION WAS EQUIVALENT TO A STATEMENT TO B. C. I. THAT CLAIMANT HAD REQUESTED ITS DRAFT TO BE CANCELLED AND THAT, FOR THAT REASON, HE WAS CANCELLING THE ADVICE. IF HE HAD EXPRESSED IN SO MANY WORDS WHAT, UNDER THE CUSTOM, HIS NOTIFICATION IMPLIED, THERE CAN BE NO DOUBT THAT HE WOULD HAVE NO RIGHT TO RETAIN THE MONEY SO PROCURED. IT IS SUBMITTED THAT THE FACT THAT THE REPRESENTATION IS SUPPLIED BY THE UNIVERSAL CUSTOM, INSTEAD OF BY EXPRESS LANGUAGE, DOES NOT CHANGE THE RESULT.**

**B.**

**THE STATEMENT IN THE OPINION THAT "NEITHER THE RESPONDENT NOR THE PURCHASER OF THE CHECK COULD KNOW" OF THE DRAFTS PAYABLE ACCOUNT, IS, WE SUBMIT, ERRONEOUS, AS A MATTER OF LAW.**

The undisputed testimony is that there was a general, universal custom for the foreign bank, on receipt of the advice of the drawing of a draft, to charge K. N. & K.'s account with the amount thereof and to credit the same amount to its own Drafts Payable account. The custom being admitted, no one would be heard to plead ignorance of it; it would be an implied term of every transaction whether the parties were, in fact, mindful of it, or

not. In these circumstances, it is respectfully submitted that the court should not have *presumed* that respondent and the original purchaser of the draft did not know it—*and this is particularly so with respect to Respondent, which, being a bank, would certainly be presumed to know the customs of the banking business?*

Consequently, we submit, there was no "general understanding" that K. N. & K. had the right to cancel drafts advised "when they saw fit to do so"; that they did not remain "master" of the moneys which had been transferred to the Drafts Payable Account to pay drafts advised and that this money did not remain "subject to the bankrupts' control." The only evidence in the case is to the contrary. Furthermore, we submit this Court's assumption that neither respondent nor the original payee had knowledge that the fund would be credited to the Drafts Payable Account of B. C. I. to await the presentation of the draft is contrary to the undisputed evidence in the case.

If we be correct in the foregoing, the Trustee has no right to hold the moneys which the B. C. I. returned to the Receiver upon his representation, contrary to the fact, that he was entitled to it.

## II.

**The relations of the parties to each other are fixed by a carefully drawn written contract, prepared by K. N. & K. In this contract it is expressly provided that respondent shall draw its own drafts on foreign banks and then supply K. N. & K. with funds "to cover"; that "promptly" upon receipt of this money K. N. & K., "as agents of the drawer", will provide the drawee with funds "to cover". K. N. & K. themselves describe their relation to the transaction as "Transfer Agents". The emphasis placed by respondent in its argument upon particular phrases picked out from the varous steps in the course of the performance of this contract seems to have obscured the provisions of the contract itself, with the result that the prevailing opinion appears to be based upon inferences as to the general import of the transaction which are, in fact, contrary to that stated in and clearly deducible from the written contract. Respondent does not rely upon phrases that can be picked out from the several steps to change or override the general import of the transaction, as shown by the terms of the contract; on the contrary, these phrases are incidents in the performance of the contract and are perfectly consistent with its expressed general import. Respondent asks only that the "general import of the transactions", as shown by the contract, be given effect; that K. N. & K. be held to be what the parties stated, in their contract, they were intended to be, *i. e.*, "Transfer Agents".**

In the concluding paragraph of the prevailing opinion it is said:

> "The decision of this case depends more upon the general import of the transaction and upon what the parties were likely to want than upon the phrases that can be picked out from the several steps."

If this were a case arising out of an "over-the-counter" transaction—a case in which there were no express contract to point out the general import of the transaction—the Court would, of course, be obliged to infer that the intent and desire of the parties, though unexpressed, was similar to that which usually exist in transactions of the same general nature, and a phrase here or there, inconsistent with that intention, would not be permitted to override the recognized general import of such transactions. Such, for instance, was the *Beecher* case in Massachusetts, cited in the opinion of the Court, in which the presence of the word "agent" in a *receipt*, given for money which was apparently paid over the counter to some clerk for *the purchase of a money order*, was held not to create an agency. There was no express contract there providing for an agency and the general nature of the transaction—an over-the-counter purchase of a money order—inherently negatived an agency. Ours, however, was not an "over-the-counter" transaction. It was not a transaction of a nature which inherently negatives an agency; neither is it a case in which the intent and desire are left to inference. Here we have a carefully worked out written contract, couched in language selected by K. N. & K., in which the contracting parties have recorded in precise terms "the general import of the transaction" and "what the parties wanted". Nothing in the nature of the transaction suggests that the intent was different from the one expressed *in the contract*, to

wit: that K. N. & K. act merely as *"Transfer Agents"* and

> "are employed merely *as the agents of the drawers* for the purpose of advising the issue of their drafts and providing the drawee bank with sufficient funds to cover their payment".

These clauses, and others in the contract to the same effect, coupled with the fact that K. N. & K. would not undertake the employment unless the said "sufficient funds to cover", as well as their compensation for their services, were first put into their hands, make it clear, we submit, that the general import of the transaction was that the respondent was to furnish K. N. & K. with money which K. N. & K., as respondent's "agents", were to "transfer" to the foreign bank for the payment of a draft which the respondent had drawn on that bank.

*What other agency could possibly be involved?*

The prevailing opinion states that K. N. & K. were to provide for payment "as convenient to themselves". It is, of course, true that they could accomplish the transfer by

> "transfer of credit from our balance or otherwise",

but this referred only to the *method* in which they would make the transfer. The *result* they were employed to accomplish, *i. e.*, provide the drawee

> "with suffcient funds to cover",

and the *time* in which they were to make the transfer, *i. e.*, "at once", are fixed by the contract.

The respondent is not seeking, by the phrases that can be picked out from the several steps following the making of the contract, to place upon the relations of the

parties a status different from that expressly provided for in the contract. On the contrary, respondent respectfully points out that the phrases which appear in these several steps are consistent with, and confirmatory of, the relation provided for in the contract.

When respondent sent its money to K. N. & K. as "Transfer Agents" and K. N. & K., upon the receipt thereof, "at once" notified B. C. I. of the drawing of the respondent's draft and, "as agent of the drawer", provided B. C. I. with a fund "to cover the draft" so advised, these acts were consistent with the relation which the contract created. K. N. & K. knew that B. C. I. would, immediately upon receipt of that advice, credit the necessary amount to the Drafts Payable Account, an account representing moneys set aside by B. C. I. to await the presentation of drafts advised, and that K. N. & K.'s "agency" would thereupon have been carried out.

Never as long as K. N. & K. were in business did they take a position inconsistent or in conflict with the relation described in the written contract. "Promptly" and "at once" after the receipt of claimant's money they created the fund to pay the draft and they never did a single act to indicate that they had any further relation to that money. They recognized they had no right to interest on it; they no longer treated it as an asset of theirs; they were not interested to know whether the draft was ever presented; they had no right to a re-credit of the amount unless the drawer cancelled the draft and requested them to so notify B. C. I. These facts are consistent with the duties and obligations of the parties under the contract and establish clearly the intention of the parties to set aside and specifically appropriate the sum necessary to meet the draft. The fact that K. N.

& K. created the fund abroad out of their balance with B. C. I. is immaterial. The controlling fact is they *did* create it and thereupon it became the fund for the payment of claimant's draft.

**IF K. N. & K. HAD MADE A SEPARATE REMITTANCE TO B. C. I. OF THE SPECIFIC AMOUNT REQUIRED TO PAY CLAIMANT'S DRAFT, WITH INSTRUCTIONS TO B. C. I. TO CREDIT DRAFTS PAYABLE ACCOUNT WITH THAT AMOUNT AND HONOR THE DRAFT, AND B. C. I. HAD MADE THE TRANSFER, THE ASSIGNMENT OF THAT MONEY FOR THE PURPOSE OF PAYING THE DRAFT WOULD BE CLEAR.**

We submit that the mere fact that instead of making the separate specific remittance, K. N. & K. accomplished the same result by a transfer of their credit does not change the result.

In the prevailing opinion it is stated:

> "Of course, there is room for difference if the parties did not express very clearly what they wanted or meant * * *."

We respectfully submit they did express clearly what they wanted and what they meant. However, if the desire and intention had not been expressed "very clearly," the doubt would have to be resolved against the Trustee. The contract was drawn by K. N. & K.

11. Upon the grounds aforestated, Respondent respectfully prays for a rehearing herein.

Respectfully submitted,

Wm. De Forest Manice,
*Counsel for Petitioner.*

## Certificate of Counsel.

STATE OF NEW YORK, }
COUNTY OF NEW YORK, } ss.:

WILLIAM DE FOREST MANICE, being duly sworn, deposes and says:

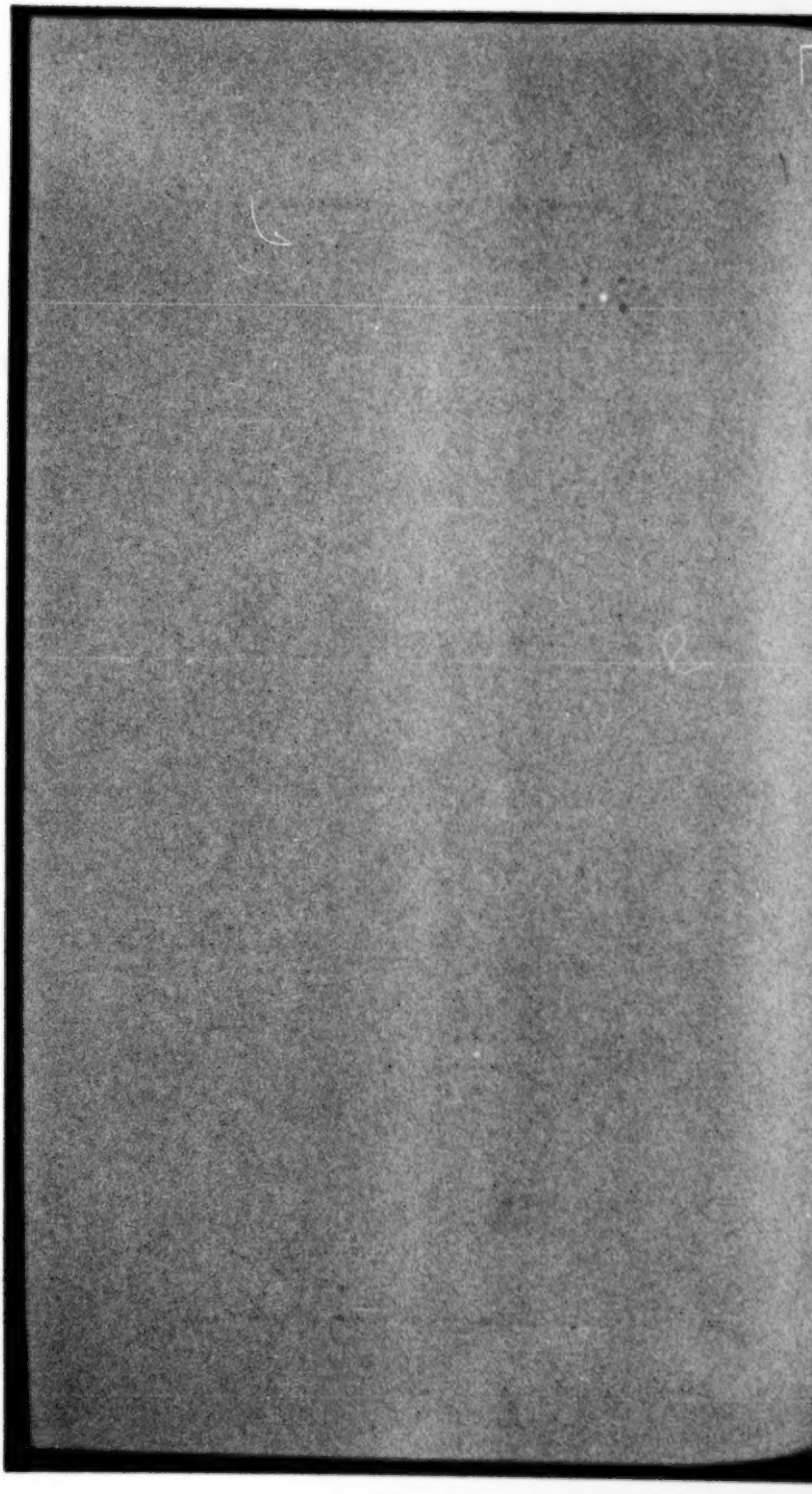
That he is counsel for the First National Bank of Trinidad, Colorado, Respondent, and that the foregoing Petition for Rehearing is presented in good faith and not for delay.

WILLIAM DE FOREST MANICE.

Sworn to before me this }
24th day of January, 1928. }

LILLIAN M. CALL.
[SEAL.] Notary Public, N. Y. Co. Clerk's No. 401
Reg. No. 9441
Commission expires March 30, 1929.

[redacted]



# INDEX.


PAGE

MOTION ..... 1

STATEMENT OF THE CASE ..... 2

BRIEF ..... 4

I—The moneys were received by the bankrupts to be applied to a particular purpose and were received and held in a fiduciary capacity ..... 4

II—Under the circumstances of this case and as between these parties, there was a completed equitable assignment or irrevocable declaration of trust when the bankrupts notified the foreign bank of the drawing of the draft and instructed it to honor the same and charge their account ..... 7

CONCLUSION—The decree of the Circuit Court of Appeals should be affirmed ..... 17

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PAGE

Averetts' Adm'r v. Booker, 15 Gratt. 163 ..... 15

Bickerdike v. Bollman, 1 Term. Rep. 405 ..... 5
Brill v. Tuttle, 81 N. Y. 454 ..... 14, 15

Clegg v. Cotton, 3 Bos. & P. 239 ..... 5
Coates v. First National Bank, 91 N. Y. 26 ..... 13

Dickins v. Beal, 10 Pet. 572 ..... 6

Eastman Koslak Co. v. National Park Bank, 231 Fed. 320, affirmed 247 Fed. 1002 ..... 11, 12

Farley v. Turner, 26 L. J. Ch. 710 ..... 5
Fourth Street National Bank v. Yardley, 165 U. S. 634 ..... 12
French's Executrix v. Bank of Columbia, 4 Cranch 141 ..... 6

In re Gubelman (Petition of Munteanu), 13 Fed. (2nd) 730 ..... 8

Mazukiewicz v. Hanover National Bank, 240 N. Y. 317 ..... 6
Merchant's Bank v. State Bank, 10 Wall. 604 ..... 5
Munger v. Shannon, 61 N. Y. 251 ..... 14, 17

The Bank of the United States v. The United States, 2 How. 711 ..... 15

White's Bank v. Myles, 73 N. Y. 335 ..... 15


## STATUTES CITED.


Commercial Laws of the World, Vol. 25, p. 481 ..... 15

Uniform Negotiable Instruments Law, Secs. 1, 3 .... 14

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| | PAGE |
|---|---|
| Aigler, 38 Harvard Law Review, 857 | 13 |
| Corpus Juris, Vol. 5, p. 913 | 9 |
| Corpus Juris, Vol. 8, p. 123 | 14 |
| Corpus Juris, Vol. 8, p. 686 | 6 |
| Daniel, Neg. Instr., Vol. 2, Sec. 1596 | 5 |
| Lawyers' Reports, Annotated, Vol. 35, p. 647 | 14 |
| Pomeroy, Equity Jurisprudence, Vol. 3, Sec. 1282 | 9 |
| Stone, 21 Columbia Law Review, 510 | 5 |
| Story, Eq. Jurisprudence, Vol. 2, Secs. 1045, 1046 | 9, 10 |
| Williston on Contracts, Vol. 1, Secs. 425, 426 | 9, 14 |

# Supreme Court of the United States

OCTOBER TERM—1926.

No. 661.

THE EQUITABLE TRUST COMPANY OF NEW YORK, as Trustee in Bankruptcy of Knauth, Nachod & Kuhne,
Petitioner,

against

FIRST NATIONAL BANK OF TRINIDAD, COLORADO,
Respondent.

APPEAL FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

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## MOTION FOR PERMISSION TO FILE A BRIEF AS AMICUS CURIAE IN THE ABOVE-ENTITLED CAUSE ON BEHALF OF FIDELITY TRUST COMPANY OF NEW YORK, HAVING A SIMILAR CLAIM AGAINST THE BANKRUPT ESTATE.

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*To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:*

COMES NOW Fidelity Trust Company of New York, by its counsel, requesting permission to file the following brief as amicus curiae in the above-entitled cause.

## Statement.

This is a review on a writ of certiorari of a decision of the Circuit Court of Appeals, Second Circuit, reversing an order of the District Court for the Southern District of New York, and remanding the cause with instructions to grant the above-named respondent a priority in its claim against the estate of the bankrupts.

The bankrupts, Knauth, Nachod & Kuhne, were international bankers. As part of their business they offered what they called a "Drawing Service," pursuant to which banks throughout the United States acquired the "privilege" of using the world-wide facilities of the bankrupts for carrying on a foreign exchange business (fol. 419). The American banks issued as principals their own drafts (supplied in blank form by the bankrupts) on any of the banks named in the bankrupts' list of correspondents, paying funds to the bankrupts, who undertook, "as the agents of the drawers," to advise the drawees and provide funds for the payment of the drafts. Pursuant to this Drawing Service, First National Bank of Trinidad drew a draft on an Italian bank for 24,360 lire, and delivered to the bankrupts $1,191.20, to be used for the payment of said draft. The bankrupts duly notified the Italian bank of the drawing of the draft and requested it to charge same to their account, and the Italian bank thereupon charged the account of the bankrupts with the amount of the draft and credited the amount to a "Drafts Payable" account. Before the draft was presented for payment, a petition in bankruptcy was filed against Knauth, Nachod & Kuhne, and a receiver was appointed, who instructed the Italian bank not to pay the draft, and pursuant to his direction the Italian bank subsequently recredited all amounts standing in their Drafts Payable account which

had not been paid, and remitted the amount thereof to the receiver. The draft was thereafter presented to the Italian bank and dishonored, and was returned to the purchaser, who collected the amount thereof from the respondent and delivered the said draft to the respondent.

On the hearing before a Special Master it was stipulated that a large number of other banks had similar claims.

In behalf of the claimant it was contended, first, that the moneys remitted to the bankrupts were received by them as agents of the remitter for the purpose of applying the same to the payment of the draft, and, second, that there was an equitable assignment by the bankrupts of the moneys on deposit by them with the Italian bank for the payment of the draft. The Special Master held that the bankrupts did not receive the money as agents of the remitter or in a fiduciary capacity, and that there was not an equitable assignment. The District Court confirmed the report of the Special Master. The Circuit Court of Appeals reversed on the ground that the agreement to transfer the credit, followed by its actual transfer, provided a fund which the drawee was obliged to devote to the payment of the draft, and created an equitable assignment or an irrevocable declaration of trust by the bankrupts, and in view of that ruling found it unnecessary to consider the claimant's first point, whether the bankrupts originally received the claimant's check in a fiduciary capacity.

The Fidelity Trust Company of New York is not one of the banks included in the above-mentioned stipulation.

Pursuant to the Drawing Service conducted by the bankrupts, the Fidelity Trust Company of New York drew a draft on an English bank and remitted the required moneys to the bankrupts, who duly advised the English bank of the drawing of the draft and instructed it to honor the draft and charge their account. There is, how-

ever, this difference in the situation of Fidelity Trust Company of New York. The English banks, unlike the banks of most of the continental countries, did not, on receipt of such advice, charge the account of Knauth, Nachod & Kuhne and credit the amount to a Drafts Payable account. They merely sent a form letter acknowledging receipt of the advice. In all other respects the situation was the same. It is the contention of the Fidelity Trust Company of New York that the decision of the Circuit Court of Appeals should be affirmed, but on a broader ground that that assigned by that Court. It is our contention that there was a completed equitable assignment or irrevocable declaration of trust when Knauth, Nachod & Kuhne, having received the moneys from the remitter, notified the drawee bank of the drawing of the draft and instructed it to pay the draft out of their moneys on deposit, and that while the entries in the books of the drawee bank may fortify the conclusion reached in the case at bar, they were not essential to the completeness of the equitable assignment or declaration of trust, and that such assignment or declaration of trust depended upon the acts of the parties to the Drawing Service, and did not depend upon the book entries made abroad by the bank on which the draft was drawn.

## BRIEF.

### I.

### The moneys were received by the bankrupts to be applied to a particular purpose and were received and held in a fiduciary capacity.

The respondent contends that moneys remitted to the bankrupts, in connection with the drawing of a draft under

the terms and provisions of the bankrupts' Drawing Service, were received by the bankrupts as agents of the remitter for the purpose of applying the same to the payment of the draft, and were therefore held in trust, and that when the fund abroad was returned to the receiver, he held it upon the same trust that the bankrupts held the original remittance. We align ourselves with the argument of the respondent on this point. In their Drawing Service the bankrupts expressly held themselves out to their customers as acting in the capacity of "agents" for the purpose of advising the issue of the drafts and providing the drawee bank with funds to cover their payment. It is entirely unnecessary to hold that the technical relation of principal and agent existed. As held in the leading case of *Farley* v. *Turner*, 26 L. J. Ch. 710, and as pointed out by Mr. Justice Stone in his article in 21 Columbia Law Review 510, it is enough that the moneys were paid to the bankrupts to be used to meet the draft drawn in accordance with the terms of the Drawing Service, and that the bankrupts before the filing of the petition in bankruptcy had appropriated the moneys to their undertaking for account of the drawer by notifying the drawee of the drawing of the draft and requesting the drawee to honor it and charge their account.

We submit that this is not an ordinary case of the purchase of foreign exchange or an ordinary case where money is paid to a foreign exchange house in return for its agreement to provide funds in a foreign country. It has long been considered that it is a *fraud* to draw a check when there are no funds of the drawer in the hands of the drawee (*Bickerdike* v. *Bollman*, 1 Term. Rep. 405; *Clegg* v. *Cotton*, 3 Bos. & P. 239; *Merchant's Bank* v. *State Bank*, 10 Wall. 604; 2 *Daniel, Neg. Instr.*, Sec. 1596), although the rule is qualified to this extent—that even if the drawer has no money in the hands of the drawee, still if a check

be drawn under such circumstances as to induce the drawer to entertain a reasonable expectation that it will be paid, he has not committed a fraud and will be entitled to due presentment and notice of dishonor (8 *Corpus Juris* 686; *Mazukiewicz* v. *Hanover Nat. Bank*, 240 N. Y. 317; *French's Executrix* v. *Bank of Columbia*, 4 Cranch 141; *Dickins* v. *Beal*, 10 Pet. 572).

When the First National Bank of Trinidad, Colorado, or the Fidelity Trust Company of New York drew its check to the order of a customer upon a bank located in Europe, it represented that it had sufficient funds in that bank or had made appropriate arrangements for the payment thereof. Doubtless the average man who buys a check drawn by an American bank on a foreign bank assumes that the American bank has drawn against funds on deposit in the foreign bank. In drawing such a check and making the implied representation of funds available abroad, the American banks relied upon the Drawing Service offered them by Knauth, Nachod & Kuhne. Pursuant to the terms of that service they paid over the money which they had received from their customers (retaining only a trifling commission) to Knauth, Nachod & Kuhne, relying upon their promise to forward promptly their advice of the draft and provide the drawee with funds sufficient for the payment thereof, acting as agents of the drawer (fols. 422-423). We submit that this was not an ordinary contract relation, and that Knauth, Nachod & Kuhne assumed a fiduciary obligation to perform the duties expressly assumed by them as "agents of the drawer" and to exonerate the drawer from the implication of fraud.

## II.

**Under the circumstances of this case and as between these parties, there was a completed equitable assignment or irrevocable declaration of trust when the bankrupts notified the foreign bank of the drawing of the draft and instructed it to honor the same and charge their account.**

We submit that the assignment or irrevocable declaration of trust was complete upon receipt by the foreign bank of the instructions given by the bankrupts, regardless of the entries made by the drawee on its books. This question was not presented to the Circuit Court of Appeals. In the case at bar, it appeared that the drawee, upon receipt of the advice, had actually charged the account of the bankrupts with the payment of the draft and credited the same to a Drafts Payable account. Indeed, it is the undisputed testimony in this case that this is a universal custom (fol. 348), although that is contrary to the fact. The Circuit Court of Appeals naturally referred to such entries by the drawee as an additional make-weight, and, of course, if the making of such entry was in accordance with the universal custom, it would be unimportant to consider the effect of such notification and instructions standing alone, without the support of the book entries. We submit that the fact that the drawee charged the account of the bankrupts on its books is not controlling, and that the equitable assignment or irrevocable declaration of trust found by the Circuit Court of Appeals would result, irrespective of the entries made by the drawee on its books.

The same Court refused to say that the actual transfer of the credit was a "vital distinction."

> *In re Gubelman* (Petition of Munteau), 13 Fed. (2nd) 730, 732.

In the Court below, Judge Hand first pointed out that even if the bankrupts remained liable after they had posted the advice to the drawee and the drawee had made the necessary entries on its books, they could so finally and completely devote the fund to the payment of the draft as to create themselves constructive trustees for the benefit of the holder, and then went on to say:

> "It is, however, proper to observe that if, as we think, the bankrupts did not remain liable after performance, their action in advising the drawee to transfer the credits was more plainly a final appropriation of the deposit than it would otherwise have been. On such a view, by those acts they had acquitted themselves of all their obligations, and certainly the contract intended that they should secure payment of the draft. If they secured it at all, it must have been when they did the last necessary act. As a make-weight, therefore, we give our reasons for saying that the limit of their obligation was to secure the entries upon the drawee's books."

It seems to have been the opinion of Judge Hand that when the bankrupts notified the drawee of the drawing of the draft and requested it to honor the same and charge their account, the bankrupts appropriated the funds abroad to the benefit of the holder and assumed a fiduciary relation. The Court of Appeals found it unnecessary to consider the claimant's first point, i. e., whether the bankrupts *originally* received the claimant's check in a fidu-

ciary capacity, but in discussing the question as to the possible effect of the Italian law, Judge Hand said:

> "The question is whether the bankrupts made themselves constructive trustees of their claim against the drawer; that question depends upon the law of the place where the supposed trustees acted. We cannot regard the making of the entries as the declaration of trust, even though without them the appropriation would have been incomplete. The bankrupts' fiduciary relation to the deposit was created by the contract, and by their appropriation of their funds to the benefit of the holder. These took place here. The drawee's compliance with their orders was at most only a condition * * *."

It seems strange that the relations between the drawer and Knauth, Nachod & Kuhne, dependent upon the contract between them, should be affected one way or the other by the action of the foreign bank, over which neither had any control. If the bankrupts held the moneys of the First National Bank of Trinidad upon an irrevocable trust, why should it be said that the Fidelity Trust Company of New York is in worse plight merely because the Italian banks were accustomed to make certain entries on their books on receipt of advice from the bankrupts, whereas the English banks were not accustomed so to do?

Knauth, Nachod & Kuhne were creditors of the foreign bank. They gave the debtor an order requesting it to pay the draft drawn by the American bank. An order by the creditor, given directly to the debtor, requesting him to pay a third person, is an assignment of the claim if the third person is notified of it by the creditor's procurement or acts upon it.

3 *Pomeroy, Equity Jurisprudence*, Sec. 1282.
5 *Corpus Juris*, 913.
1 *Williston on Contracts*, Sec. 426.
2 *Story, Equity Jurisprudence*, Secs. 1045, 1046.

The case at bar should be dealt with in the same way as though the drawer bank were the third person mentioned in the authorities. The American bank acted in reliance on the promise of Knauth, Nachod & Kuhne to order the foreign bank to pay the draft. When the order was given, the appropriation was absolute, and the American bank or the holder of its draft could avail of the trust in equity without reference to the assent or dissent of the mandatory. The Circuit Court of Appeals held that the bankrupts' fiduciary relation to the deposit was created by the contract and by their appropriation of their funds for the benefit of the holder of the draft. We contend that the appropriation was complete without the making of the entries by the foreign bank; but even if, without those entries, the appropriation would have been incomplete, the fact remains that by their acts the bankrupts assumed a fiduciary relation to the deposit in the hands of the foreign bank. Those funds were affected by a trust for the benefit of these drafts, and the funds so held in trust did not pass as part of the bankrupt estate and were wrongfully taken by the receiver in bankruptcy.

It has sometimes been said that the true test whether or not an absolute appropriation has been made out depends upon the point at whose risk the property is.

2 *Story, Equity Jurisprudence*, Sec. 1045.

Judge Hand, in the case at bar, expresses the opinion that the bankrupts did not remain liable after performance, that is, after the drawee set up the credit in favor of the holder. We submit that the obligation of the bankrupts was to provide funds for the payment of the draft, advise the drawee and instruct it to honor the draft. The acceptance of such instructions may be evidenced by book entries, or by letter of acknowledgment (as in the case of English banks), dependent upon the local banking cus-

tom. The bankrupts, in their drawing service, undertook to advise the drawee of the issue of drafts and provide the drawee with sufficient funds to cover their payment (fol. 423), but did not undertake to cause the drawee to make certain entries on its books. If the question is, upon whom would the loss fall in the event of the failure of the drawee bank, we submit that the drawer would have to look to the drawee from the time that the bankrupts performed their contract obligation by notification to the drawee, and that the bankrupts' performance was not dependent upon the making of book entries by the drawee bank.

The trustee in bankruptcy has sought to derive support from those cases which establish the rule that in the ordinary case where a check is drawn upon a bank account, followed by a letter of advice to the drawee bank instructing it to pay the check, there is no assignment. Such a case is *Eastman Kodak Co.* v. *National Park Bank*, 231 Fed. 320, affirmed 247 Fed. 1002. Cases of this type are, however, clearly distinguishable from the case at bar. In those cases the relationship is the ordinary one between depositor and banker. That is not true in the case at bar; nor in the case at bar is the claim based primarily upon the draft in question, but rather upon a contract relationship between the claimant and the bankrupts pursuant to which the instrument was drawn. Furthermore, in those cases, it was attempted to establish an assignment for the purpose of imposing liability upon the drawee bank. Whether or not the holder of the draft here in question had a cause of action against the foreign drawee bank need not concern this Court. The claim in suit is not against the drawee bank, but against Knauth, Nachod & Kuhne, a party whose name does not even appear on the instrument. The very cases laying down the rule that there is no assignment in the usual case of the drawing of a check,

followed by a letter advice, recognize that the rule is limited to cases of negotiable instruments where there are no distinguishing features.

> *Eastman Kodak Co.* v. *National Park Bank* (*supra*), at page 323.

This Court has held that where it was the understanding of the parties that a particular fund should be charged, equity will enforce such an intention as against parties charged with notice.

In *Fourth Street National Bank* v. *Yardley*, 165 U. S. 634, this Court said:

> "*As between a check holder and the bank upon which such check is drawn*, it is settled that, unless the check be accepted by the bank, an action cannot be maintained by the holder against the bank.
>
> It is also settled that *a check, drawn in the ordinary form does not, as between the maker and payee*, constitute an equitable assignment *pro tanto* of an indebtedness owing by the bank upon which the check has been drawn, and that the mere giving and receipt of the check do not entitle the holder to priority over general creditors in a fund received from such bank by an assignee under a general assignment made by the debtor for the benefit of his creditors.
>
> That the owner of a chose in action or of property in the custody of another may assign a part of such rights, and that an assignment of this nature, if made, will be enforced in equity, is also settled doctrine of this court. * * *
>
> Whilst an equitable assignment or lien will not arise against a deposit account *solely* by reason of a check drawn against the same, *yet the authorities establish that if, in the transaction connected with the delivery of the check it was the understanding and agreement of the parties that an advance about to be made should be a charge on and be satisfied*

> *out of a specified fund a court of equity will lend its aid to carry such agreement into effect* as against the drawer of the check, mere volunteers, and parties charged with notice." (Italics ours.)

This Court, in the same opinion, quoted with approval from *Coates* v. *First National Bank*, 91 N. Y. 26, where it was said:

> "* * * when in addition to the check there was an oral agreement between the drawer and payee, by which the former, for a valuable consideration, agreed to assign so much of the indebtedness of the bank to him as was represented by the check, and the check was given to enable the payee to collect and recover the portion of the debt assigned, the agreement operated as an assignment, and was sufficient to vest in the payee a title to that portion of the debt."

The principle that checks are not assignments is strictly limited by the facts of the particular case. This is made clear by an examination of the authorities collated by Professor Ralph W. Aigler in an article on "Rights of Holder of Bill of Exchange Against the Drawee," 38 Harvard Law Review 857.

Not only is the principle of these cases inapplicable to the case at bar because of the distinguishing characteristics already referred to, but the very form of the draft in suit takes this case out of the application of a principle which, at best, is limited to negotiable instruments. The form of the draft in question serves to substantiate the contention that as between the claimant and the bankrupts there was an assignment.

Each of these instruments reads as follows:

> "Pay from balance against this check * * *."

On its face, the draft was payable only from a certain unspecified "balance." An order which specifically requests payment out of a particular fund to which the drawer is entitled is construed as an assignment. An ordinary check is not an assignment because it is an order to the drawee to pay the sum ordered irrespective of the condition of the drawer's account. The essential question is whether a fund is referred to as merely a possible source of reimbursement for the drawee or whether the order is to be paid only from the fund (Uniform Negotiable Instruments Law, Secs. 1, 3; 1 *Williston on Contracts*, Sec. 425; 8 *Corpus Juris* 123; cases cited in Note, 35 L. R. A. 647).

The leading case in New York is *Munger* v. *Shannon*, 61 N. Y. 251. In that case, DWIGHT, C., writing for the Court, said:

> "The true test would seem to be whether the drawee is confined to the particular fund, or whether, though a specified fund is mentioned, he would have the power to charge the bill up to the general account of the drawer, if the designated fund should turn out to be insufficient. In the final analysis of each case, it must appear that the alleged bill of exchange is drawn on the general credit of the drawer."

In all cases in which a particular fund is designated in a draft and the language is ambiguous, the turning point is whether it was the intention of the parties that the payment should be made only out of the designated fund or whether the direction to the drawee to pay was intended to be absolute and the fund was mentioned only as a source of reimbursement or as a direction as to bookkeeping.

*Brill* v. *Tuttle*, 81 N. Y. 454, 457.

The same test is applied in the Federal Courts (*The Bank of the United States* v. *The United States*, 2 How. 711).

An order requesting the drawee to pay a sum of money "out of any moneys in his hands belonging to me" was held to be payable out of a particular fund and not to be a negotiable bill of exchange.

*Averetts' Adm'r* v. *Booker*, 15 Gratt. 163.

Counsel for the trustee has stated in a brief submitted to the Circuit Court of Appeals that the draft used was "very carefully drawn" to comply with the German Check Law (25 Commercial Laws of the World, 481), which requires that a check shall contain a direction addressed by the drawer to the drawee to pay a certain sum "*out of his property.*" Of course, the provisions of the German Check Law are entirely immaterial in the case at bar; the draft having been drawn in Colorado, payable in Italy. On its face it permits payment only from "balance against this check." Since the intention and understanding of the parties is material in establishing the nature of the instrument (*White's Bank* v. *Myles*, 73 N. Y. 335; *Brill* v. *Tuttle*, 81 N. Y., at p. 462), it does not follow that the instrument must be given the same effect in every situation and as against every party. The question before this Court has to do solely with the rights of the drawers as against the bankrupts. There is no need to consider the effect which should be given to these instruments in favor of or as against parties not involved in the case at bar.

The drawer had no balance whatever. The instrument was drawn on a form prepared by the bankrupts and furnished as part of their drawing service. While the American bank drew the checks, they were on these blank forms and were actually drawn on the funds of the bankrupts, and, as between the drawer, the drawee and the bankrupts,

were payable solely from the bankrupts' balance on deposit. It is not to be assumed that the drawee bank was authorized to pay on the personal credit of the *drawer*, because the drawer was entirely unknown to the drawee. There is nothing to show that the drawee could pay on the personal credit of the *bankrupts*, because the check was payable "from balance."

As a matter of fact, the checks supplied by the bankrupts under their drawing service were of a uniform color and appearance, and would be recognized by any of the bankrupts' correspondents as Knauth, Nachod & Kuhne checks. Under the circumstances, the language, "Pay from balance against this check," as between the drawer, the drawee and Knauth, Nachod & Kuhne, could have but one meaning, namely, "Pay from Knauth, Nachod & Kuhne's balance against this check." As between these parties, the instrument was, therefore, payable out of a particular fund.

Viewing the entire transaction as a whole, we submit that each draft, drawn as it was by authority of the bankrupts, should, as against the bankrupts' trustee, be construed as an assignment by the bankrupts of a sum of money on deposit with the foreign bank.

The equitable assignment resulting from the acts of the bankrupts was not revocable by them or by their receiver or trustee in bankruptcy.

> "Considering the transaction as an equitable assignment, it was irrevocable in equity as soon as it was delivered to the holders, and at law as soon as it was assented to by the defendant, so far as to require him to appropriate so much of the profits as were equal to the amount of the note, to its payment. (*Mcnomy* v. *Ferrers*, 3 J. R. 71-83; *Peyton* v. *Hallett*, 1 Caines 363; *Canfield* v. *Mooper*, 12 J. R. 346; 2 Story Eq. Jur., sec. 1044.) The principle of these cases is that in equity the fund is held in trust

for the creditor, and that he has an equitable lien upon it for the amount of his debt. * * * Even in a court of law though an order of this kind might be revocable until assented to, yet, after assent by the parties, the creditor's rights would become so fixed that the drawer could no longer revoke his direction (*Williams* v. *Everett*, 14 East. 581)."

*Munger* v. *Shannon*, 61 N. Y. 251, at p. 258.

## CONCLUSION.

The moneys withdrawn by the trustee in bankruptcy from the foreign bank did not pass as part of the bankrupt estate because the money was originally received by the bankrupts in a fiduciary capacity, because there was a completed equitable assignment or irrevocable declaration of trust of the funds on deposit and because as between the parties before the Court the draft itself had the effect of an assignment. In arriving at these conclusions, the fact that a bookkeeping entry was or was not made by the drawee bank is not controlling.

The decree of the Circuit Court of Appeals should be affirmed.

Respectfully submitted,

HAROLD NATHAN,
Counsel for Fidelity Trust Company of New York.

# SUPREME COURT OF THE UNITED STATES.

No. 130.—October Term, 1927.

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| The Equitable Trust Company of New York, Trustee in Bankruptcy of Knauth, Nachod & Kuhne, Petitioner, vs. The First National Bank of Trinidad, Colorado. | On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit. |

[January 3, 1928.]

Mr. Justice Holmes delivered the opinion of the Court.

Knauth, Nachod and Kuhne being in bankruptcy, the respondent, The First National Bank of Trinidad, Colorado, claimed priority in respect of certain funds collected by the trustee in bankruptcy, the petitioner, from the Banca Commerciale Italiana; the ground of the claim being that these funds were charged with a trust in the hands of the Italian bank. The respondent prevailed in the Circuit Court of Appeals. 13 F. (2d) 732. A writ of certiorari was granted by this Court. 273 U. S. 684.

The facts are as follows. The bankrupts had credit with many foreign banks and to enable small banks in this country to issue drafts upon such banks in their own name offered these terms: "Upon receipt of advice of draft, accompanied by adequate funds payable at par in New York, we shall promptly forward our advice of the same and provide the drawee with funds sufficient for the payment of the draft abroad, by a transfer of credit from our balance, or otherwise, provided the draft is drawn on a bank named in our latest list of correspondents." It was added that the drawing banks act as principals and draw in their own name, the bankrupts being employed merely "as agents of the drawers for the purpose of advising the issue of their drafts and providing the drawee banks with sufficient funds to cover their payment."

The bankrupts sent out lists of their foreign correspondents and also daily rate cards fixing the rate for the various foreign currencies, including their own compensation, good only for the day of the date. In accordance with this plan the Trinidad bank drew a draft on a branch of the Banca Commerciale Italiana for 24360 lire, sent notice to the bankrupts that they had sold it "and shall thank you to protect same upon presentation," and remitted therewith a check for $1,191.20, which the bankrupts received on May 22, 1923, and deposited to their general account. On the same day the bankrupts sent to the Italian bank and to its branch a list and description of the drafts issued by inland banks and by the bankrupts and requested it to "honor the above listed drafts charging same to our account." The list was received on or before June 4, 1923; the account of the bankrupts was debited with the total amount and to that extent ceased to draw interest, the bank getting its compensation in this way. At the same time an account termed "Drafts Payable" was credited with the same amount, this account being credited in the same way with drafts from other dealers with the bank and the bankrupts themselves. In accordance with the practice in international banking, the bankrupts when they saw fit to do so cancelled their advices and were recredited in their general account; and although in fact they did not cancel the advice of inland drafts except when requested by the inland banks, the Italian bank did not know or inquire into reasons and so far as appears the Trinidad bank or at all events the holder of the draft knew nothing of the mode of bookkeeping described.

The draft was presented after the petition in bankruptcy had been filed and was dishonored; the petitioner as drawer had to take it up and now claims on the two grounds that the sum paid by it was paid upon trust to be applied to the draft, and that as holder of the draft it is, by subrogation, an equitable assignee of the bankrupts' deposit with the drawee. The first of these need not detain us. *Beecher* v. *Cosmopolitan Trust Co.*, 239 Mass. 48, *Legaiti* v. *The Mechanics & Metals National Bank*, 230 N. Y. 415. The identity of the fund was not maintained and no one expected it to be. See *National City Bank* v. *Hotchkiss*, 231 U. S. 50, 56, 57. The bankrupts undertook to 'forward' advice but only to 'provide' the drawee with funds. The second contention was that which prevailed below. Of course there is room for difference

if the parties did not express very clearly what they wanted or meant but we are led to a different conclusion whether the reliance be upon the rights of the holder or upon the original contract between the respondent and the bankrupts. In the first place the ignorance of the whole affair on the part of the holder and the general understanding that the party dealing immediately with the bank having the 'Bills Payable' account is master of it, as between himself and the bank, are quite inconsistent with the notion that an entry on that account is the appropriation of a fund to the holder's use. The respondent tries to give a different turn to the evidence but the master's finding and our own conclusion from the testimony leave no doubt in our minds. It is true that after such an entry the interest allowed to the depositor stops but that is only a convenient way of giving compensation to the bank. It is not uncommon in commercial transactions to see some of the elements of an earlier or a half imitated transaction appear, although the essentials of the transaction are not there. Whether a fund was appropriated or not depended wholly on the dealings between the bankrupts and the Italian bank; and both of them dealt with the account as subject to the bankrupt's control. The cessation of interest was for the benefit of the bank because the account was only with its general funds, and did not have any assets especially set aside and appropriated to it—in short was a bookkeeping device for the convenience of the bank.

Again, the terms offered by the bankrupts to their correspondents seem to us to promise the appropriation of a specified fund to the draft as little as they promise to apply the money received by them to that end. They are to provide the drawee banks with sufficient funds for the payment of the drafts by transfer of credit from our balance 'or otherwise'. They are to provide, that is, as convenient to themselves, for payment by the drawee banks, not to give them an earmarked corpus to be handed over. They are requested by their correspondents to protect the drafts, which again means merely to see that they are paid. *Wabash, St. Louis & Pacific Ry. Co.* v. *Ham*, 114 U. S. 587, 596. People dealing with large banks do not ordinarily seek the ambiguous security of an identified fund, they are satisfied if the bank gives them credit. We see no indications that the Trinidad bank was not perfectly

content to know that it would have credit with the Banca Commerciale, and that in the usual course of things its drafts would be paid. Evidently with this conception of their duties the bankrupts asked the Italian bank "to protect to the debit of our account the drafts" in question and others, and the branch bank to "honor the above listed drafts." That such a letter of advice is not an assignment is clearly explained in *Eastman Kodak Co.* v. *National Park Bank*, 231 Fed. Rep. 320, 323; (affirmed, 247 Fed. Rep. 1002.)

We have called the instrument under which the respondent claims as assignee, a draft. But on its face it is called 'check'. The form was a general form furnished by the bankrupts and the purpose is said to have been that in continental Europe or some parts of it checks are not subject to the same stamp tax as drafts. It is said in a reputable work that the fact that the instrument purports to be drawn upon a deposit is what constitutes it a check. Daniels, Negotiable Instruments, 6th ed., § 1569. The existence of this opinion sufficiently explains the words of the document before us 'Pay from balance against this check'. They no more purport to assign a fraction of a fund than does an ordinary check. They would not naturally take that shape as the respondent, the drawer of the check, had no fund in the hands of the drawee.

The decision of this case depends more upon the general import of the transaction and upon what the parties were likely to want than upon the phrases that can be picked out from the several steps. We repeat that in our opinion what the parties meant to establish and what the respondent got was the assurance of a credit abroad to the extent of its check as in the case of a letter of credit, not an attenuated property right in an account to which no special funds were attached and the particulars of which neither the respondent nor the purchaser of the check could know.

*Order reversed.*

A true copy.

Test:

*Clerk, Supreme Court, U. S.*

# SUPREME COURT OF THE UNITED STATES.

No. 130.—October Term, 1927.

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| The Equitable Trust Company of New York, as Trustee in Bankruptcy of Knauth, Nachod & Kuhne, Petitioner, *vs.* The First National Bank of Trinidad, Colorado. | On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit. |

[January 3, 1928.]

Mr. Justice Stone, dissenting.

The agreement of the bankrupts, on the faith of which petitioner sold its draft, did more than stipulate that the draft should be paid on presentation. It provided specifically the method of payment; that the bankrupts should "promptly", on notice of the draft, "provide the drawee with funds sufficient for the payment of the draft abroad, by a transfer of credit or otherwise." It plainly contemplated the course of business, actually followed, in which a credit, to be established with the drawee, was to be set apart and specifically appropriated to the payment of the draft. The draft was by its terms made payable from "balance against this Check".

We need not discuss what the petitioner's rights would have been if no such credit had been established, for here the bankrupts had performed their contract fully and to the letter. They set apart the stipulated credit. Withdrawal of it by them would have been a violation of their contract with petitioner, for the contract contained no intimation of a right to revoke it, and if the receiver had not done what they had no right to do the draft would have been paid. Nor does it appear to me that the real question is whether the Italian bank was charged with a trust with respect to funds lodged with it by the bankrupts. It may be assumed that it was not a trustee, but only a debtor to the bankrupts for the funds thus received, with power to discharge the debt *pro tanto* by payment of the draft when presented.

Stated with precision the question seems rather to be whether, since the bankrupts had performed their agreement by specifically designating and setting apart enough of their credit with the Italian bank to meet the draft, the credit thus set apart is to be treated in equity as security for the payment of the draft. If subject to that equitable obligation, neither the bankrupts nor the receiver could convert the credit, so set apart, into cash and turn the proceeds over to general creditors freed of that obligation.

Since *Holroyd* v. *Marshall*, 10 H. L. Cas. 191, it has been generally accepted doctrine, the recording acts permitting, that an agreement to hold property which the promisor may afterward acquire as security for the payment of a debt, operates in equity once the property is acquired, to give the stipulated security to the promisee in preference to general creditors. Such is the rule in this Court. *Sexton* v. *Kessler*, 225 U. S. 90. I had supposed it to be equally well settled that the agreement need not mention the word "security" to accomplish that result, if its plain purpose is to provide for the satisfaction of a debt or obligation out of identifiable property. Compare *Walker* v. *Brown*, 165 U. S. 654; *Ingersoll* v. *Coram*, 211 U. S. 335; *Hurley* v. *Atchison, Topeka & Santa Fe Ry.*, 213 U. S. 126; *Ketchum* v. *St. Louis*, 101 U. S. 306; *Parlin & Orendorff Implement Co.* v. *Moulden*, 228 Fed. 111; *Curtis* v. *Walpole Tire & Rubber Co.*, 218 Fed. 145. There has been no dissent from the view that an agreement to apply a designated credit or account to the payment of a check or draft drawn upon it creates security in the credit enforcible in equity as against general creditors. *Fourth Street Bank* v. *Yardley*, 165 U. S. 634; *Farley* v. *Turner*, 35 L. J. Ch. 710; *Coates* v. *First National Bank*, 91 N. Y. 20; *Muller* v. *Kling*, 209 N. Y. 239; *In re Hollins*, 215 Fed. 41. Equity, in making such agreements effective, does no more than it habitually does in compelling the performance of an agreement to give a mortgage to secure advances made on the faith of the agreement.

Both parties to this transaction knew that American drafts drawn on European banks would be worthless unless definite arrangement for their payment by the drawee was made in advance of their presentation, and that where, as here, a particular credit was set apart for that purpose the utility of such drafts would

be seriously impaired if the credit, once established, could be cancelled at will. No intelligent banker would sell such drafts if the establishment of such a credit were not contemplated. A bank here, drawing and selling such drafts against a credit to be established abroad by others, pledges its own credit to the payee and is secured against loss and the dishonor of its drafts only in so far as it may insure the creation of the appropriate credit and retain the benefit of it once it is created. The stipulation that the bankrupts should promptly set apart a credit for that purpose upon receipt of advice of the draft and advise the drawee of it was a material inducement to petitioner to pledge its own credit by the sale of its draft. Once performed it is valuable security to both payee and drawer, if it is permitted to have the legal sanctions which ordinarily attach to agreements of this character.

The evidence in this case appears to me, as it did to the court below, to fall far short of establishing a practice or custom, or any rule of Italian law, permitting the depositor, while the drafts are outstanding, to cancel or control for his own purposes the credit set apart for their payment. Our own rule is that a bank of deposit may not, with impunity, ignore the known equitable rights of others to the credit established by its depositor, *National Bank* v. *Insurance Co.*, 104 U. S. 54, and it would seem that that rule should be applied here in determining the rights of the parties in the absence of proof of any other. But in any case, such control, if retained by the bankrupts as between themselves and the Italian bank, could not be rightfully exercised in violation of their contract with petitioner.

The case would therefore seem to be a proper one for the application of the rule announced by this Court in *Fourth Street Bank* v. *Yardley*, *supra*, that a court of equity will lend its aid to carry into effect an agreement that an obligation shall be satisfied out of a specified credit. Applied here that rule would make effective the intention of the parties and give stability to a large and important class of banking transactions. The judgment should be affirmed.

Mr. Justice McReynolds joins in this dissent.